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In the Supreme Court of the United States

OCTOBER TERM, 1979

ELMER B. STAATS, COMPTROLLER GENERAL OF THE UNITED STATES, AND UNITED STATES OF AMERICA,
PETITIONERS

v.

BRISTOL LABORATORIES DIVISION OF BRISTOL-MYERS COMPANY

PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE SECOND CIRCUIT

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QUESTION PRESENTED

Whether, with respect to negotiated government contracts, the Comptroller General is authorized by law to examine the contractor's books and records pertaining to costs of research and development, advertising and promotion, distribution, and administration, where such costs, although not allocated by the contractor to particular products or calculated on a product basis in determining price, are defrayed by the contractor from commingled general revenues that include the government's payments under the contract.

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PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE SECOND CIRCUIT

The Solicitor General, on behalf of the Comptroller General of the United States and the United States of America, petitions for a writ of certiorari to review the judgment of the United States Court of Appeals for the Second Circuit in this case.

OPINIONS BELOW

The opinion of the court of appeals (App. A, *infra*, 1a–4a) is reported at 620 F.2d 17. The opinion of the district court (App. B, *infra*, 5a–12a) is reported at 428 F. Supp. 1388.

JURISDICTION

The judgment of the court of appeals was entered on March 25, 1980 (App. C, *infra*, 13a–14a). On June 12, 1980, Mr. Justice Marshall extended the time for filing a petition for a writ of certiorari to and including August 22, 1980. The jurisdiction of this Court is invoked under 28 U.S.C. 1254 (1).

STATUTORY PROVISIONS INVOLVED

1. 10 U.S.C. 2313(b) provides:

> Except as provided in subsection (c), each contract negotiated under this chapter shall provide that the Comptroller General and his representatives are entitled, until the expiration of three years after final payment, to examine any books, documents, papers, or records of the contractor, or any of his subcontractors, that directly pertain to, and involve transactions relating to, the contract or subcontract.

2. 41 U.S.C. 254(c) provides:

> All contracts negotiated without advertising pursuant to authority contained in this Act shall include a clause to the effect that the Comptroller General of the United States or any of his duly authorized representatives shall until the expiration of three years after final payment have access to and the right to examine any directly pertinent books, documents, papers, and records of the con-

tractor or any of his subcontractors engaged in the performance of and involving transactions related to such contracts or subcontracts. Under regulations to be prescribed by the Administrator, however, such clause may be omitted from contracts with foreign contractors or foreign subcontractors if the agency head determines, with the concurrence of the Comptroller General of the United States or his designee, that the omission will serve the best interests of the United States. However, the concurrence of the Comptroller General of the United States or his designee is not required for the omission of such clause—

(1) where the contractor or subcontractor is a foreign government or agency thereof or is precluded by the laws of the country involved from making its books, documents, papers, or records available for examination; and

(2) where the agency head determines, after taking into account the price and availability of the property or services from United States sources, that the public interest would be best served by the omission of the clause.

If the clause is omitted based on a determination under clause (2) a written report shall be furnished to the Congress. The power of the agency head to make the determination specified in the preceding sentences shall not be delegable.

STATEMENT

1. In 1973 and 1974, respondent Bristol Laboratories entered into three contracts with the Defense Supply Agency of the Department of Defense and one contract with the Veterans Administration for the sale of pharmaceutical products to the government. All four

were negotiated fixed-price contracts,[1] with a total price of approximately $2 million (App. B, *infra*, 6a–7a; C.A. App. 100–104).[2] As required by 10 U.S.C. 2313(b)[3] and 41 U.S.C. 254(c),[4] each of the contracts contained a standard access-to-records provision in which respondent agreed that "the Comptroller General of the United States or any of his duly authorized representatives shall, until the expiration of three years after final payment under this contract * * *, have access to and the right to examine any directly pertinent books, documents, papers, and records of the Contractor involving transactions related to this contract" (App. B, *infra*, 6a–7a; C.A. App. 101, 103).

Pursuant to these statutory and contractual provisions, the Comptroller General, by letter of August 26, 1974, made a timely request to Bristol for access to

> all books, documents, papers and other records directly pertinent to the contracts, which include, but are not limited to (1) records of experienced costs including costs of direct materials, direct labor, overhead, and other pertinent corporate costs, (2) support for prices charged to the Government, and (3) such other information as may be necessary for use to review the reasonableness of the contract prices and the adequacy of the protection afforded the Government's interests.

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[1] A negotiated government contract is a method of procurement authorized by statute to be used in situations in which the formal public advertising and bidding procedure is deemed impractical or unnecessary. See 10 U.S.C. 2304(a); 41 U.S.C. 252(c).

[2] "C.A. App." refers to the joint appendix filed by the parties in the court of appeals.

[3] See page 1, *supra*. This provision is applicable to the Defense Supply Agency contracts.

[4] See pages 1–2, *supra*. This provision is applicable to the Veterans Administration contract.

App. B, *infra*, 7a–8a; C.A. App. 71–72. In reply, respondent offered to make available "(1) Bristol's contract files which included shipment and invoice records, (2) records and data relating to manufacturing costs assigned by the firm to the products purchased under the contracts, and (3) Bristol's product prices to its non-Federal customers" (C.A. App. 81). However, respondent declined to produce "records concerning costs incurred for activities such as research and development, marketing and promotion, distribution and administration * * * [on the ground that] such costs are not assigned to individual products and records concerning these costs are not pertinent to the cited contracts" (*ibid.*). Respondent also refused to provide "records relating to the methodology and decisions involved in the firm's establishment of prices for the products purchased under the contracts" (*ibid.*). By letter dated March 6, 1975, the Comptroller General advised respondent that its proposal failed to satisfy the legal requirements under which the GAO request had been made (*id.* at 82).

2. On March 18, 1975, respondent commenced the present action in the United States District Court for the Southern District of New York seeking declaratory and injunctive relief against the Comptroller General (C.A. App. 24–28).[5] The United States later intervened as a defendant and filed a counterclaim to gain access to the records requested by the Comptroller General (C.A. App. 42–50).[6]

Respondent conceded in the district court that it was obligated "to provide access to records of its manufacturing costs, records which relate to the pricing of

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[5]Jurisdiction was asserted by respondent under 28 U.S.C. 1331, 1332, 1337, 2201–2202, and 5 U.S.C. 702 (C.A. App. 26).

[6]Jurisdiction over the counterclaim was based on 28 U.S.C. 1345 (C.A. App. 43).

the products delivered and records required to verify all data obtained during the course of the review" (App. A, *infra*, 8a). On this basis, it agreed to allow inspection of records pertaining to "the following items, which it lists as factors taken into account in setting prices to the government: manufacturing costs (including raw and packaging materials, labor and fringe benefits, quality control and supervision); manufacturing overhead (including plant administration, production planning, warehousing, utilities and security); royalty expenses; and delivery costs" (*ibid.*). However, respondent "strenuously resist[ed] producing data with respect to research and development, marketing and promotion, distribution and administration * * *" on the ground that these costs, which respondent neither allocated to particular products or contracts nor considered in setting the price charged to the government, "are too remote to the contracts and have only the most general relation, if any, to the prices charged" (*id.* at 8a–9a).

Following discovery, the district court granted respondent's motion for summary judgment and denied the cross-motion of the government (App. B, *infra*, 5a–12a).[7] The court rejected the government's argument that, with respect to respondent's unallocated costs, the access-to-records provisions authorized examination of "all costs met in whole or in part from revenues earned on the federal contracts * * *" (*id.* at 9a). Since respondent's unallocated costs "are pooled and met out of gross revenues * * * [consisting of] revenues from government contracts * * * co-mingled

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[7] The parties' initial motions for summary judgment were denied because of uncertainties concerning respondent's accounting methods (App. B, *infra*, 6a n.1; C.A. App. 18–23). These cross-motions were renewed after completion of the necessary discovery.

with revenues from non-government contracts," the court expressed its concern that the position urged by the government would mean that "there are no excludable records" and that respondent would be required "to make available virtually all of its books and records * * * because * * * government dollars * * * contribute to the fund from which all of the company's expenses are paid" (*id.* at 9a–10a). The court concluded that such a result would be "inconsistent" with the "words of limitation" in the access-to-records provisions authorizing the Comptroller General to examine "'directly pertinent * * * records * * * involving transactions related to [the] contract'" (*id.* at 10a; emphasis omitted); in the court's view, "[t]he reasonable assumption is that if Congress had wished to condition the receipt of a fixed-price negotiated contract on the contractors' agreement to allow such unusual and unfettered government inspection of their business records, it would have done so explicitly" (*ibid.*). In addition, the court held as a matter of contract law that "[t]he government's position is particularly unrealistic" because, in construing "the intent and understanding of the parties * * *, [i]t is inconceivable that [respondent], or any contracting firm, could have understood this clause to authorize the sweeping power of inspection claimed by the GAO" (*id.* at 10a–11a). Accordingly, the court sustained respondent's position as "a responsible and reasonable effort to distinguish 'directly pertinent' matter within the meaning of the access to records clause. It represents a sensible point at which to draw the line" (*id.* at 12a).

3. On the government's appeal, the court of appeals affirmed in a per curiam opinion for the reasons given by the district court (App. A, *infra*, 1a–4a).[8] The court

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[8] After both parties had initially appealed, the court of appeals remanded the case for consideration of respondent's request for

of appeals also noted that two intervening decisions of the Seventh Circuit had "reject[ed] the holding of the court below," but it did "not find their reasoning persuasive" (*id.* at 3a). See *Eli Lilly & Co.* v. *Staats*, 574 F.2d 904 (7th Cir.), cert. denied, 439 U.S. 959 (1978); *United States* v. *Abbott Laboratories*, 597 F.2d 672 (7th Cir. 1979).

REASONS FOR GRANTING THE PETITION

1. As the court of appeals recognized (App. A, *infra*, 3a–4a), its decision in this case conflicts with the decisions of the Seventh Circuit in *Eli Lilly & Co.* v. *Staats*, 574 F.2d 904, cert. denied, 439 U.S. 959 (1978), and *United States* v. *Abbott Laboratories*, 597 F.2d 672 (1979). All of these cases arose out of identical demands by the Comptroller General, under identical access-to-records provisions, for cost data pertaining to pharmaceutical products supplied to the government pursuant to negotiated fixed-price contracts. The Seventh Circuit in *Eli Lilly* expressly declined to follow the decision of the district court in the instant case (574 F.2d at 913) and ordered the contractor to make available the type of cost records denied to the Comptroller General here. By the same token, the Second Circuit, in affirming the district court in this case, explicitly rejected the *Eli Lilly* holding.[9]

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a protective order. Upon the consent of the parties, the district court approved a protective order on September 6, 1979 (App. A, *infra*, 3a n.2; C.A. App. 184–187). Thereafter, only the government pursued its appeal. No issue is presented in this petition concerning the need for or scope of an appropriate protective order.

[9]The decision below also conflicts in principle with *Hewlett-Packard Co.* v. *United States*, 385 F.2d 1013 (9th Cir. 1967), cert. denied, 390 U.S. 988 (1968). In that case, GAO "requested all books, documents, papers or records 'relating to the pricing

Resolution of the conflict by this Court is warranted. The Second and Seventh Circuits have disagreed on the proper construction of access-to-records provisions that, by statute, are applicable to virtually all of the government's negotiated procurement contracts throughout the country.[10] However, the ability of the Comptroller General to fulfill his assigned duties ought not depend on the location of the contractor or the venue of a lawsuit. In the present situation, forum shopping is encouraged, since contractors have an incentive to file suit in the Second Circuit whenever possible. What is more, the existing conflict is likely to hinder contractors' voluntary cooperation with GAO and to lead to further litigation in other circuits. For these reasons, the Court should review the decision of the court of appeals in this case.[11]

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and cost of performance, support for prices charged to the Government, and such other necessary information which would permit * * * [GAO] to review the reasonableness of the contract prices * * * ' " (385 F.2d at 1015). The district court granted the government's motion for summary judgment "and entered a judgment substantially as prayed for in the complaint" (385 F.2d at 1013–1014) declaring that GAO "could examine any such records 'relating to the cost of producing the items furnished by Hewlett-Packard Company under the aforesaid contracts, including costs of direct material, direct labor and overhead costs * * * ' " (385 F.2d at 1016). The court of appeals affirmed, holding that these costs "directly pertain to * * * [the contract], because if out of line with the contract price, the contract may have been an inappropriate means of meeting this particular procurement need of the Government" (*ibid.*).

[10] In fiscal year 1979, the total value of negotiated government contracts was approximately $78 billion. See Office of the Secretary of Defense, *Military Prime Contract Awards for Fiscal Year 1979*, Table 9; General Services Administration, *Procurement by Civilian Executive Agencies for Fiscal Year 1979*, Part I.

[11] The issue presented in this petition is currently pending in two other circuits. In *SmithKline Corp.* v. *Staats*, 483 F. Supp.

2. The court of appeals has misconstrued the access-to-records provisions and unduly restricted the Comptroller General's authority to promote sound government procurement practices. By failing to consider the purpose and legislative history of the provisions and to defer to GAO's interpretation that has been recognized by Congress, the court of appeals erred.

The inspection provisions in 10 U.S.C. 2313(b) and 41 U.S.C. 254(c) were enacted in 1951 as amendments to the Armed Services Procurement Act of 1947 and the Federal Property and Administrative Services Act of 1949. See Pub.L. No. 82-245, ch. 652, 65 Stat. 700. The Committee Reports expressed Congress' determination that "negotiated contracts * * * require close supervision and control * * *." H.R. Rep. No. 82-791, 82d Cong., 1st Sess. 2 (1951); S. Rep. No. 82-603, 82d Cong., 1st Sess. 2 (1951). Congressman Hardy, the sponsor of the legislation, explained that examination of contractors' records by the Comptroller General would enable "the Government Accounting Office to look behind the * * * [price] which had been established * * * [to assess whether it was] excessive" and would act as a "safeguard against waste and extravagance" in government procurement. 97 Cong. Rec. 13198 (1951). See also *id.* at 13373 (remarks of Rep. Hoffman) ("GAO is * * *the most effective agency we have against fraud and extravagance and waste and all those things"). As Congressman Hardy emphasized:

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712 (E.D. Pa. 1980), appeal pending, No. 80-1464 (3d Cir. filed Mar. 19, 1980), the court, although aware of the district court's decision in this case (*id.* at 719), "agree[d] with *Eli Lilly's* reasoning" (*id.* at 722). On the other hand, in *Merck & Co.* v. *Staats*, Civil Action No. 74-1447 (D.D.C. Aug. 12, 1977), appeal pending, Nos. 79-1435, 79-1438 (D.C. Cir. argued Feb. 11, 1980), which was decided prior to the court of appeals' decision in *Eli Lilly*, the court found "persuasive" and was "guided" by the district court's decision in the present case (slip op. 4-5).

> The major purposes of this bill are twofold: One, to give the Comptroller General the proper tools to do the job the Congress has instructed him to do; and, two, to provide a deterrent to improprieties and wastefulness in the negotiation of contracts.

Id. at 13198; see also *id.* at 13200 (remarks of Rep. Hardy). Congress "clearly understood * * * that there are a lot of other situations besides those involving fraud which might be uncovered" (*id.* at 13199) (remarks of Rep. Hardy). Because of its concern that "there is every chance in the world that the Government will come out on the short end of the deal," Congress enacted the access-to-records statutes to "enable the * * * [Comptroller General] to check the transaction, both from the Government records and the contractors' books" (*id.* at 13198) (remarks of Rep. Hardy).[12]

Prior to the decision in this case, the courts of appeals had broadly construed the access-to-records provisions to effectuate this congressional intent. As the court explained in *Hewlett-Packard*, *supra*, the Comptroller General is empowered to investigate whether a contractor's costs are "out of line with the contract price" and hence whether "the contract may have been

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[12] Congressman Hardy's bill did not originally contain the provision that records be "directly" pertinent. The word "directly" was added as a floor amendment offered by Congressman Hoffman, who explained that "[t]he purpose is to limit the 'snooping' that may be carried on under this bill * * *." 97 Cong. Rec. 13377 (1951). Congressman Hardy did not object to this modification, which passed without debate or discussion. In these circumstances, we do not believe that Congressman Hoffman's amendment significantly altered the scope or intendment of Congressman Hardy's bill or bars the Comptroller General's access to records legitimately needed to protect the government against waste, excessive prices, and ineffective procurement. See *Eli Lilly*, *supra*, 574 F.2d at 916 & n.8

an inappropriate means of meeting this particular procurement need of the Government" (385 F.2d at 1016). Similarly, in *Eli Lilly, supra,* the court of appeals followed "the broad reading of *Hewlett-Packard* * * * [as] most consistent with the plain meaning of the statutory language and with the legislative history" (574 F.2d at 913), and concluded that Congress envisioned "an inquiry [by the Comptroller General] into whether costs are excessive" (*id.* at 915). In departing from this understanding, the Second Circuit's decision frustrates the statutory objective and defeats the intention of Congress.

It is not a valid objection that the Comptroller General has sought access to records of costs that respondent does not allocate to individual products.[13] The government cannot be bound by the accounting method respondent has established for its own purposes. Cf. *Exxon Corp.* v. *Department of Revenue of Wisconsin,* No. 79-509 (June 10, 1980), slip op. 12-14. Moreover, respondent's election to keep its business records on the basis of unallocated costs cannot obscure the fact that an analysis of these costs is necessary for the Comptroller General to determine whether the price charged the government is fair and reasonable. To operate profitably, respondent must recover its costs from sales revenues, and it uses the payments by the government under the contracts at issue here, as part of commingled general revenues, to help to defray its unallocated expenses (C.A. App. 164, 166-169).[14] As the court of appeals explained in

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[13] It does appear, however, that respondent, by setting its prices in part on the basis of its historical pricing and that of its competitors, takes into account its unallocated costs (C.A. App. 137, 158, 164-166).

[14] The government was charged respondent's normal wholesale price (C.A. App. 158).

Eli Lilly, supra, the "inclusion [of unallocated costs] in the price of the product [purchased by the government] is not unforeseeable once the costs are incurred. * * * The mere fact that, as [respondent] asserts, it does not or even could not allocate costs such as research and development to an individual contract does not undercut the proposition that those costs are directly pertinent to an individual contract but merely indicates that they are directly pertinent to more than one individual contract" (574 F.2d at 914). Especially where, as in the pharmaceutical industry, "manufacturing and distribution costs of individual * * * products have been estimated to constitute as little as 9 per cent of the products' sale prices" (*id.* at 913) and manufacturers expend approximately 12 percent of sales revenues on research and development (C.A. App. 107), it is manifest that the Comptroller General's inquiry into the appropriateness of the contract price cannot be limited to allocated costs of production and delivery and must include such significant unallocated costs as research and development, marketing and promotion, distribution, and administration.[15]

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[15] Of course, insofar as respondent has allocated a given category of costs, the Comptroller General would be entitled to examine only such costs that have been attributed to the product supplied the government (together with records necessary to verify such data). To the extent that broader access is required, it is the result of respondent's decision not to allocate its costs and the consequent need for the Comptroller General to construct a measure of those costs in order to determine the reasonableness of the contract price. Whatever the nature of a contractor's accounting system, the Comptroller General's authority remains the same—to examine those costs necessary to determine whether the contract price was "extravagan[t]," "excessive," or "wasteful[ ]" (97 Cong. Rec. 13198 (1951) (remarks of Rep. Hardy)).

Moreover, GAO has consistently construed the access-to-records provisions to authorize examination of all cost records necessary to determine the reasonableness of the price charged the government, and Congress, although aware of this construction, has not indicated its disapproval of the agency's interpretation or amended the statutes to reject that position. See C.A. App. 108. In 1963, Robert Keller, General Counsel of GAO, explained GAO's "position that the contract clause and the statute give us the right to examine the cost records of the contractor and other pertinent data that relates to the items included in the contract, in sufficient completeness and detail to permit us to determine the reasonableness of the negotiated prices." *Hearings on Relation of Cost Data to Military Procurement Before the Subcomm. for Special Investigations of the House Comm. on Armed Services*, 88th Cong., 1st Sess. 10 (1963). Mr. Keller also noted that GAO's "interpretation of the statute has been consistently applied since its enactment without objection by the Congress * * * " (*id.* at 10–11). Congressman Hardy, based on his "background of personal knowledge * * * [of] what congressional intent was at the time * * * [the statutes were] originally passed" (*id.* at 3), commented that Mr. Keller had "stated this case very well as to the necessity for having a contract provision permitting audits of negotiated contracts" (*id.* at 23).

Two years later, GAO again apprised Congress of its construction of the access-to-records provisions. Comptroller General Campbell testified that these provisions "permit detailed examination of a contractor's records to insure the necessary degree of supervision and control. In other words, the clear intent of the statute is to provide for the examination by the General Accounting Office of such records of a contractor, to such an extent as will permit a meaningful

examination of the reasonableness of the prices charged to the Government." *Hearings on Comptroller General Reports to Congress on Audits of Defense Contracts Before the Subcomm. on Military Operations of the House Comm. on Government Operations*, 89th Cong., 1st Sess. 44 (1965). Mr. Campbell later reiterated GAO's position "that the contract clause and the statute on which the clause is based gives us the right to examine the cost records of the contractor and other pertinent data that relate to the items included in the contract, in sufficient completeness and detail to permit us to examine into the reasonableness of the negotiated prices" (*id.* at 45).[16] And General Counsel Keller also stated the agency's view "that the Congress intended the General Accounting Office to examine the books and records of the contractor to make certain that the Government was getting a fair deal out of negotiated contracts" (*id.* at 147).

In 1971, Congress was again advised of GAO's interpretation of the access-to-records provisions. Paul Shnitzer, Assistant General Counsel of GAO, testified that such access "is very good for the purpose of determining what costs the contractor actually incurred in the performance of the contract as compared to the contract price." *Hearings on Competitive Problems in the Drug Industry Before the Subcomm. on Monopoly of the Senate Select Comm. on Small Business*, 92d

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[16] Comptroller General Campbell's statement was clearly understood by Mr. Charles I. Derr, Senior Vice President, Machinery & Allied Products Institute, who described GAO's position to be "that the statute should be construed as broadly as is necessary in order to permit [GAO] to determine whether contract prices are reasonable" (*Hearings on Comptroller General Reports, supra*, at 513).

Cong., 1st Sess. 8018 (1971). Mr. Shnitzer then elaborated (*id.* at 8018-8019):

> What I am saying is, and we do have a case which ultimately went up as far as the Supreme Court, is that under our 1951 authority, the contract is required to include a provision which gives the GAO the right to examine records of costs, direct and indirect, generated in the performance of that contract. So if a contract is awarded to company A and it comes within the purview of this—it is a negotiated contract for, let us assume, $100,000—we would have a right then to go back and examine the records of company A—the cost records, direct and indirect, to determine how much it cost him to perform that contract * * *.

In light of this history, the court of appeals was plainly unwarranted in rejecting GAO's longstanding interpretation of the access-to-records provisions. See *Eli Lilly*, *supra*, 574 F.2d at 915. The court failed to heed the " 'venerable principle that the construction of a statute by those charged with its execution should be followed unless there are compelling indications that it is wrong * * *.' " *E.I. DuPont DeNemours & Co.* v. *Collins*, 432 U.S. 46, 54-55 (1977), quoting *Red Lion Broadcasting Co.* v. *FCC*, 395 U.S. 367, 381 (1969). And this principle is especially apt " 'when Congress has refused to alter the administrative construction' * * * [and] that construction accords with well-established congressional goals." *Board of Governors of the Federal Reserve System* v. *First Lincolnwood Corp.*, 439 U.S. 234, 248, 251 (1978), quoting *Red Lion Broadcasting Co.* v. *FCC*, *supra*, 395 U.S. at 381. Furthermore, the district court's conclusion that respondent's position appeared "reasonable" and "sensible" (App. B, *infra*, 12a) was insufficient to overcome the deference due GAO's interpretation. " 'To sustain * * * [GAO's] application of this statutory term, we

need not find that its construction is the only reasonable one, or even that it is the result we would have reached had the question arisen in the first instance in judicial proceedings.'" *Udall* v. *Tallman*, 380 U.S. 1, 16 (1965), quoting *Unemployment Comm'n* v. *Aragon*, 329 U.S. 143, 153 (1946). Rather, "[i]t is settled that courts should give great weight to any reasonable construction of a regulatory statute adopted by the agency charged with the enforcement of that statute." *Investment Company Institute* v. *Camp*, 401 U.S. 617, 626–627 (1971).

Finally, the court of appeals incorrectly relied on the presumed intentions of the parties to hold that the contractual access-to-records clause does not encompass the materials sought by the Comptroller General concerning respondent's unallocated costs. In view of the decision in *Hewlett-Packard* and GAO's public statements of its position to Congress, respondent was on notice of GAO's interpretation and cannot be assumed to have had a contrary understanding. See *Eli Lilly*, *supra*, 574 F.2d at 918. But, more importantly, the meaning of the contractual access-to-records clause does not rest on the understanding of the parties. The clause was statutorily required to be included in the contract, and its content is necessarily determined by those statutes rather than by the parties' intentions. See *e.g.*, *Federal Crop Insurance Corp.* v. *Merrill*, 332 U.S. 380, 383–385 (1947); *Dematteo Const. Co.* v. *United States*, 600 F.2d 1384, 1391 (Ct. Cl. 1979); *Jackson* v. *United States*, 573 F.2d 1189, 1194 (Ct. Cl. 1978).

CONCLUSION

The petition for a writ of certiorari should be granted.

Respectfully submitted.

WADE H. MCCREE, JR.
Solicitor General

ALICE DANIEL
Assistant Attorney General

MARK I. LEVY
Assistant to the Solicitor General

MICHAEL KIMMEL
ROBERT KAPLAN
Attorneys

AUGUST 1980

APPENDIX A

UNITED STATES COURT OF APPEALS
For the Second Circuit

SEPTEMBER TERM 1979

No. 679

ARGUED MARCH 10, 1980
DECIDED MARCH 25, 1980

Docket Nos. 77-6153

BRISTOL LABORATORIES DIVISION OF
BRISTOL-MYERS COMPANY, PLAINTIFF-APPELLEE,

against

ELMER B. STAATS, COMPTROLLER GENERAL
OF THE UNITED STATES,
DEFENDANT-APPELLANT,

-and-

UNITED STATES OF AMERICA,
INTERVENOR-DEFENDANT-APPELLANT.

Before: FRIENDLY and FEINBERG, Circuit Judges and SIFTON, District Judge.[1]

Appeal from judgment of the United States District Court for the Southern District of New York, Morris

---

[1] Honorable Charles P. Sifton of the United States District Court for the Eastern District of New York, sitting by designation.

E. Lasker, J., denying appellant United States' cross-motion for summary judgment and granting appellee's motion for summary judgment in an action for declaratory and injunctive relief limiting appellant Comptroller's access to appellee's business records.

Affirmed.

MICHAEL H. DOLINGER, Assistant United States Attorney, New York, NY (Robert B. Fiske, Jr., United States Attorney for the Southern District of New York, New York, NY, Naomi Reice Buchwald, Assistant United States Attorney, Harland F. Leathers, Attorney, Department of Justice, John G. Brosnan, Attorney, General Accounting Office, of Counsel), for Appellants Comptroller General of the United States and United States of America.

ROBERT L. SHERMAN, New York, NY (Weil, Guttman & Davis, New York, NY, Gilbert H. Weil, of Counsel), for Plaintiff-Appellee.

PER CURIAM:

The United States and Elmer B. Staats, Comptroller General of the United States, appeal from a judgment of the United States District Court for the Southern District of New York, Morris E. Lasker, J., granting the motion of Bristol Laboratories Division of Bristol-Meyers Company ("Bristol") for summary judgment and denying the government's cross-motion for summary judgment. During 1973 and 1974, Bristol entered into negotiated fixed-price contracts with the Veterans Administration and with the Defense Supply Agency of the Defense Department; pursuant to 41 U.S.C. § 254(c) and 10 U.S.C. § 2313(b), these contracts contained a clause that granted the Comptroller "access to and the right to examine any directly pertinent" business records "involving transactions related

to" the contracts. In 1974, the Comptroller formally requested Bristol to make available all records "directly pertinent" to the contracts. The parties disagreed, however, as to what records were required to be produced; accordingly, Bristol commenced an action for declaratory and injunctive relief in order to limit the Comptroller's access to its records. Judge Lasker held that the government's interpretation of the access-to-records clause incorporated in the contracts was untenable as a matter of both statutory interpretation and contractual construction. This appeal followed.[2] We affirm for the reasons given in Judge Lasker's excellent opinion, reported at 428 F. Supp. 1388 (S.D.N.Y. 1977), to which we refer the reader.

We would see no reason to say anything further except that in the unusually lengthy period between Judge Lasker's opinion and this appeal, see note 2, supra, there have been two opinions in the United States Court of Appeals for the Seventh Circuit, upon which the government relies heavily, bearing on the scope of the Comptroller's authority to examine records similar to those he seeks here. See United States v. Abbott Laboratories, 597 F.2d 672 (7th Cir. 1979); Eli Lilly & Co. v. Staats, 574 F.2d 904 (7th Cir.), cert. denied, 439 U.S. 959 (1978). These cases reject the holding of the court below, but we do not find their reasoning persuasive. We note particularly that not only was there a vigorous dissent in *Lilly*, see 574 F.2d at 918 (Pell, J., dissenting), but also that the precedential force of that decision has been weakened by

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[2] Both parties filed timely notices of appeal from Judge Lasker's order. Subsequently, a panel of this court remanded the case for consideration of Bristol's request for a protective order without prejudice to prosecution of the appeals. In September 1979, the district court approved a protective order, which had been agreed to by the parties. Only the appeal of the government is before us today.

the reluctant concurrences of two members of the *Abbott* panel, see 597 F.2d at 674 (Pell, J., concurring), 675 (Wood, J., concurring). Compare also SmithKline Corp. v. Staats, No. 75-499 (E.D. Pa. Jan. 24, 1980) with Merck & Co., Inc. v. Staats, No. 74-1447 (D.D.C. filed Aug. 12, 1977), appeal docketed, No. 79-1435 (D.C. Cir. Apr. 30, 1979); see generally Case Comment, The Comptroller General's Authority to Examine the Private Business Records of Government Contractors, 92 Harv. L. Rev. 1148 (1979).

The judgment of the district court is affirmed.

APPENDIX B

UNITED STATES DISTRICT COURT
Southern District of New York

75 Civ. 1334

MEMORANDUM 45769

BRISTOL LABORATORIES DIVISION OF
BRISTOL-MYERS COMPANY, PLAINTIFF,

against

ELMER B. STAATS, COMPTROLLER GENERAL
OF THE UNITED STATES, DEFENDANT,

and

UNITED STATES OF AMERICA,
INTERVENOR-DEFENDANT.

APPEARANCES:

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Of Counsel: GILBERT H. WEIL, ESQ.
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Of Counsel: NAOMI REICE BUCHWALD, ESQ.
Assistant United States Attorney

J. ROGER EDGAR, ESQ.
Department of Justice

JOHN G. BROSNAN, ESQ.
General Accounting Office

LASKER, D.J.

This case arises out of a dispute between Bristol Laboratories Division of Bristol-Myers Company (Bristol) and Elmer B. Staats, Comptroller General of the United States, regarding the scope of Staats' contractual right to inspect Bristol's books and records. Bristol and the United States, as intervenor-defendant, seek a declaration of their respective rights and a corresponding injunction. The parties have renewed cross-motions for summary judgment.[1] Since no disputed issues of fact remain, the case is ripe for determination.

In 1973 and 1974 Bristol was awarded three negotiated fixed-price contracts for the sale of prescription drugs to the Defense Supply Agency. Pursuant to the provisions of 10 U.S.C. § 2313(b)[2] all three contracts contain a so-called access to records clause, which in pertinent part provides:

> "[Bristol] agrees that the Comptroller General of the United States or any of his duly authorized representatives shall, until the expiration of three years after final payment under this contract . . . have access to and the right to examine any di-

---

[1] By Memorandum dated December 14, 1975 the original cross-motions were denied without prejudice because of insufficient data and the appearance of a material dispute regarding Bristol's accounting methods. The necessary discovery is now complete, and the facts have been clarified.

[2] 10 U.S.C. 2313(b) provides:

> "(b) Except as provided in subsection (c), each contract negotiated under this chapter shall provide that the Comptroller General and his representatives are entitled, until the expiration of three years after final payment, to examine any books, documents, papers, or records of the contractor, or any of his subcontractors, that directly pertain to, and involve transactions relating to, the contract or sub-contract."

> rectly pertinent books, documents, papers, and records of [Bristol] involving transactions related to this contract."

In 1973 Bristol obtained a similar contract with the Veterans Administration which, pursuant to 41 U.S.C. § 254(c),[3] contains an identical access to records clause. Final payment on all of these contracts was complete by the end of July, 1974.

By letter dated August 26, 1974 Staats formally requested Bristol to make available to him cost records relating to the four contracts. He explained that the request was one of several directed at companies which supply pharmaceuticals to federal government agencies as part of a general review of drug procurement being undertaken by the General Accounting Office (GAO). He alluded to recent attempts by the GAO to conduct a comprehensive study of pricing practices in the pharmaceutical industry and the refusal of the drug manufacturers voluntarily to supply the information requested. Staats specified that he wished to inspect certain records including

> " . . . but not limited to (1) records of experienced costs including costs of direct materials, direct labor, overhead, and other pertinent corporate costs, (2) support for prices charged to the Gov-

---

[3] 41 U.S.C. 254(c) provides:

> "(c) All contracts negotiated without advertising pursuant to authority contained in this chapter, chapter 11C of Title 5, chapter 10 of Title 40, and chapter 11 of Title 44 shall include a clause to the effect that the Comptroller General of the United States or any of his duly authorized representatives shall until the expiration of three years after final payment have access to and the right to examine any directly pertinent books, documents, papers, and records of the contractor or any of his subcontractors engaged in the performance of and involving transactions related to such contracts or sub-contracts."

ernment, and (3) such other information as may be necessary for use to review the reasonableness of the contract prices and the adequacy of the protection afforded the Government's interests." (Staats Letter, August 26, 1974; Exhibit A, Weil Affidavit).

Bristol responded that it was agreeable to providing records "deemed pertinent" to the contracts. (Purdy Letter, September 13, 1974; Exhibit B, Weil Affidavit) In the ensuing months, however, after further correspondence and meetings between GAO and Bristol personnel, it became apparent that there were irreconcilable differences regarding the proper scope of the GAO review. The differences focus on the GAO's right to examine records pertaining to the costs of research and development, marketing and promotion, distribution and administration.

Bristol agrees that it is obliged by the terms of the contracts to provide access to records of its manufacturing costs, records which relate to the pricing of the products delivered and records required to verify all data obtained during the course of the review. Accordingly, Bristol states that it is ready and willing to allow GAO personnel to inspect its books and records with regard to the following items, which it lists as factors taken into account in setting prices to the government: manufacturing costs (including raw and packaging materials, labor and fringe benefits, quality control and supervision); manufacturing overhead (including plant administration, production planning, warehousing, utilities and security); royalty expenses; and delivery costs. However, it strenuously resists producing data with respect to research and development, marketing and promotion, distribution and administration (except to the extent that these areas may be included in the factors listed above), because it claims that these costs are too remote to the contracts

and have only the most general relation, if any, to the prices charged.

The United States insists that the GAO may inspect Bristol's records with respect to any and all costs met in whole or in part from revenues earned on the federal contracts, whether or not those costs are specifically assigned by Bristol to the contracts or the products delivered. According to the government the test is simply "whether the burden of [the] costs is borne by the Government in the prices it must pay for the contract items." (Government's Memorandum, August 29, 1975 at 13)

The Government's theory has far reaching implications. The only items excludable from the Comptroller General's reach would be those, if any, which relate to the costs recovered exclusively from non-government contracts. (Government's Memorandum, August 29, 1975 at 13) It is undisputed, however, that Bristol does not separately compute the cost of government and non-government contracts or pay for them out of separate funds. Accordingly, there are no excludable records under the Government's theory. Indeed, the company does not compute the costs attributable to any particular contract. It does allocate certain direct costs, for manufacturing and overhead, by product. Records of these expenses are thus readily available and are among those the company concedes to be discoverable. Its other expenses are not allocated at all; they are pooled and met out of gross revenues. In other words, revenues from government contracts are co-mingled with revenues from non-government contracts, and the resulting fund is used to pay for all expenses. If the government's interpretation of the access to records clause is correct, Bristol will be required to make available virtually all of its books and records, because although it is impossible to trace the use of government dollars, those dollars contribute to

the fund from which all of the company's expenses are paid.

Such a result would be inconsistent with the language of the access to records clause and the statutes pursuant to which the clause was included in the contracts. The clause provides that GAO representatives may examine "*directly pertinent* books, documents, papers and records . . . *involving transactions related to* [the] contract." (Emphasis supplied) This language is taken almost verbatim from the statutes which require the clause in all fixed-price negotiated contracts. 10 U.S.C. § 2313(b) requires that all such contracts with Defense agencies must provide that the GAO may examine all records "that *directly pertain to*, and *involve transactions relating to*, the contract." (Emphasis supplied) Similarly, 41 U.S.C. § 254(c), which controls the contract with the Veterans Administration, requires that provision be made for inspection of "any *directly pertinent* books . . . of the contractor . . . *involving transactions related* to such contracts." (Emphasis supplied) All of the underscored phrases are words of limitation. It is a distortion of the language to argue that it permits GAO officials to discover virtually everything there is to know about the structure of the contractors' business. The reasonable assumption is that if Congress had wished to condition the receipt of a fixed-price negotiated contract on the contractors' agreement to allow such unusual and unfettered government inspection of their business records, it would have done so explicitly.

There is an additional important reason for rejecting the government's interpretation. Although the access to records clause has its origins in statute, it is nevertheless a contractual provision. We are thus confronted with the task of construing the contracts, a task which turns on the intent and understanding of the parties regarding the import of the access to rec-

ords clause at the time the contracts were entered. The government's position is particularly unrealistic when viewed in this light. It is inconceivable that Bristol, or any contracting firm, could have understood this clause to authorize the sweeping power of inspection claimed by the GAO. As a matter of contractual construction, the government's argument falls of its own weight.

The government's contention that Bristol is obligated to open all of its books and records for perusal was implicitly rejected by the court in *Hewlett-Packard v. United States*, 385 F.2d 1013 (9th Cir.), *cert. denied*, 390 U.S. 988 (1967), the single reported decision construing the access to records clause. The court's discussion clearly reflects its conclusion that an order granting the Comptroller General access to a contractor's books "without limitation" would contravene the limiting language in the statutes and the clause itself. 385 F.2d 1015–16.[4] In *Hewlett-Packard* the court simply ordered the contractor to make available records relating to its production costs, over the contractor's argument that this information is not "directly pertinent" to the contract because production

[4] Nor can the government draw support from the unreported decision in *Eli Lilly and Company* v. *Staats*, No. IP75-72—(S.D. Ind. Nov. 30, 1976), a case which, like the instant controversy, also grew out of Staats' attempt, in August, 1974, to use the access to records clause to obtain detailed information relating to the structure of the pharmaceutical industry. Lilly was evidently willing to disclose far less information than Bristol and presented a number of facts and legal arguments which Bristol has not put forth. The court granted Lilly's motion for summary judgment, ruling that Staats' request exceeded his authority, was of doubtful constitutionality and far exceeded the scope of the access to records clause. It permitted Staats to examine only those files and records relating specifically to the government contracts and only to the extent necessary to determine the relation between the standard catalogue price of the products and the prices charged to the government.

costs were not taken into account in arriving at the terms and conditions of the contracts in question. Since production costs are among the items Bristol has agreed to provide, the decision in *Hewlett-Packard* is of no positive aid in resolving the instant controversy.

Having rejected the government's position, it remains to determine the appropriate scope of the Comptroller General's examination. He is, of course, entitled to examine all "directly pertinent records involving transactions related to the contract." Although these words give general guidance, they do not provide answers to the specific questions which arise in the context of each case. We agree with the government that the issue should not depend entirely on a contractor's bookkeeping method, i.e., whether it does or does not assign particular costs to particular contracts or products. However, we do not understand this to be Bristol's contention. As set forth above, Bristol allocates only the direct costs of manufacture by product. These are among the costs it offers to make available, but they are by no means the limit of its offer. Rather, Bristol is willing to provide all records relating to manufacturing costs and the pricing of the products sold to the government. The specific list of items Bristol offers to make available, set forth at page 3, *supra*, appears to reflect a responsible and reasonable effort to distinguish "directly pertinent" matter within the meaning of the access to records clause. It represents a sensible point at which to draw the line.

For the foregoing reasons, Bristol's motion for summary judgment is granted, and the government's motion is denied.

Submit judgment on notice.

Dated: New York, New York
April 7, 1977.

/s/MORRIS E. LASKER
U.S.D.J.

APPENDIX C

UNITED STATES COURT OF APPEALS
For the Second Circuit

77-6153

At a stated Term of the United States Court of Appeals for the Second Circuit, held at the United States Courthouse in the City of New York, on the twenty-fifth day of March one thousand nine hundred and eighty.

Present: Hon. HENRY J. FRIENDLY
Circuit Judge

Hon. WILFRED FEINBERG
Circuit Judge

Hon. CARLES P. SIFTON
District Judge

BRISTOL LABORATORIES DIVISION OF BRISTOL-MYERS COMPANY, PLAINTIFF-APPELLEE

v.

ELMER B. STAATS, COMPTROLLER GENERAL OF THE UNITED STATES, DEFENDANT-APPELLANT,

UNITED STATES OF AMERICA, INTERVENOR-DEFENDANT-APPELLANT.

Appeal from the United States District Court for the Southern District of New York.

This cause came on to be heard on the transcript of record from the United States District Court for the

Southern District of New York, and was argued by counsel.

ON CONSIDERATION WHEREOF, it is now hereby ordered, adjudged, and decreed that the judgment of said District Court be and it hereby is affirmed in accordance with the opinion of this court with costs to be taxed against appellants.

A. DANIEL FUSARO,
Clerk

/s/ _____
by: EDWARD J. GUARDARO
Deputy Clerk

(A true copy)

/s/ROLANNE HENRY
Deputy Clerk

APPENDIX D

UNITED STATES DISTRICT COURT
Southern District of New York

Civil Action No.
75 CIV 1334 (MEL)
JUDGMENT

BRISTOL LABORATORIES DIVISION OF
BRISTOL-MYERS COMPANY, PLAINTIFF,

-against-

ELMER B. STAATS, COMPTROLLER GENERAL
OF THE UNITED STATES, DEFENDANT,

and

UNITED STATES OF AMERICA,
INTERVENOR-DEFENDANT.

The plaintiff, Bristol Laboratories Division of Bristol-Myers Company, having duly moved for an order directing the entry of summary judgment in its favor and against the defendant, Elmer B. Staats, Comptroller General of the United States, and the intervenor-defendant, United States of America, and the intervenor defendant, United States of America, having cross-moved for an order directing the entry of summary judgment in its favor, and said motions having regularly been submitted to this Court on the 15th day of November, 1976, and this Court having rendered a memorandum decision dated April 7, 1977 granting plaintiff's motion for summary judgment and denying intervenor-defendant's motion, and directing that judgment be submitted on notice, it is therefore

ORDERED, ADJUDGED AND DECREED

(1) That the motion for summary judgment of the intervenor-defendant, United States of America, be, and the same hereby is denied.

(2) That the motion for summary judgment of the plaintiff, Bristol Laboratories Division of Bristol-Myers Company, be, and the same hereby is granted in all respects.

(3) That the Comptroller General and all persons representing him or acting under his direction and authority or acting in concert or participation with him, have no right to make any efforts or take any steps to gain access to or to examine any of plaintiff's books, documents, papers or records, or to seek access to or examine any of plaintiff's books, documents, papers or records, except for 1) those containing manufacturing costs (including raw and packaging materials, labor and fringe benefits, quality control and supervision); manufacturing overhead (including plant administration, production planning, warehousing, utilities and security); royalty expenses and delivery costs of the products delivered pursuant to government contracts identified as DSA 120-73-D-1769, V797P-5929b, DSA 120-74-C-2404 and DSA 120-74-C-2724, whether or not those costs are assigned by plaintiff to any of the said contracts or products; 2) those relating to the pricing of the products delivered pursuant to said government contracts, whether or not those costs are assigned by plaintiff to any of the said contracts or products; and 3) those required to verify the data obtained in the course of the review.

(4) That the Comptroller General and his representatives shall not have access to or the right to examine any books, documents, papers, and records of Bristol relating to expenses incurred for research and development, advertising and promotion; general and

administrative and distribution except as those expenses come within the scope of the preceding paragraph.

(5) That the Comptroller General or a duly authorized representative or representatives of him may have access to those of plaintiff's books, documents, papers or records permitted by paragraph (3) herein, at the premises of plaintiff, Syracuse, New York, at a time that is mutually convenient to plaintiff and the Comptroller General, on prior notice to plaintiff of at least two weeks.

(6) That the counterclaim of intervenor-defendant, United States of America, be, and the same hereby is, dismissed.

Dated: New York, New York
July 13, 1977.

s/ MORRIS E. LASKER

U.S.D.J.

JUDGMENT ENTERED 7/15/77

/s/RAYMOND F. BURGHARDT
Clerk

A True Copy

RAYMOND M. BURGHARDT,
Clerk

BY WM MULLIGAN
Deputy Clerk

☆U.S. GOVERNMENT PRINTING OFFICE: 1980 323376 21

No. 80-264

In the Supreme Court of the United States

OCTOBER TERM, 1980

ELMER B. STAATS, Comptroller General of the United States,

and

UNITED STATES OF AMERICA, PETITIONERS

v.

BRISTOL LABORATORIES DIVISION OF BRISTOL-MYERS COMPANY

ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE SECOND CIRCUIT

JOINT APPENDIX

Petition for writ of certiorari filed August 21, 1980.
Certiorari granted December 8, 1980

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Relevant Docket Entries
United States District Court, Southern District of New York

STAATS. VS. BRISIES DIVISION OF BRISTOL-MYERS COMPANY Vs. STAATS, U.S.

75 Civ 1334 JUDGE LASKER

DATE	NR.	PROCEEDINGS
		Page #2
03-18-75	1	Filed Complaint and Issued Summons.
4-7-75	2	Filed Summons with Marshal's return. Served: Elmer B. Staats Comp. Gen of US Wash. D.C. by Certified Mail Receipt #161650 dated 3-19-25 U.S. Atty Gen. Wash. D.C. by Certified Mail Receipt #161651 dated 3-19-75 U.S. Atty Office Foley Sq. by P. Trior on 3-19-75.
5-20-75	3	Filed Deft.'s Answers.
5-28-75	4	Filed U.S. Atty's Notice of Motion for an order granting leave to the USA to intervene . . . . . ret. 6-11-75 at 10am rm 2903.
5-28-75	5	Filed U.S. Atty's Memo of Law in support of its motion to intervene.
6-24-75	6	Filed Consent Order that the U.S.A. may intervene as a party deft in this action and that the U.S.A. is directed to file its pleading within 10 days of the signing of this order . . . . Lasker, J. mn
6-30-75	7	Filed Memo-End on back of motion filed 5-28-75 . . . . Motion granted in accordance with consent order of 6-24-75 . . . It is so ordered . . . . Lasker, J. mn
6-30-75	8	Filed Deft's Objections to pltff's 1st Set of interrogs.
6-30-75	9	Filed Deft's Answers to pltff's 1st set of interrogs.
7-3-75	10	Filed ANSWER to complt by Intervenor (U.S.A.).
7-22-75	11	Filed pltffs notice of motion & Rule ((g) statement for summary judgment. Ret. 8-1-75.
7-22-75	12	Filed affdvt in support of motion for summary judgment.

DATE	NR.	PROCEEDINGS
7-22-75	13	Filed pltffs memo of law in support of motion for summary judgment.
7-25-75	14	Filed Pltff's Reply to Counterclaim of intervenor-deft.
8-14-75	15	Filed Stip & Order adj Pltff's motion for summ judge from 8-14-75 to 8-28-75 . . . . . Lasker, J.
8-29-75	16	Filed Govt-USA's Notice of Motion for an orderpur to 56 FRCP awarding summ judg to U.S. . . . . ret. 9-10-75 . . . at 10am.
8-29-75	17	Filed USA's Memo of Law in support of Motion for summ judg.
8-29-75	18	Filed Exhibit to USA's Memo of Law.
10-1-75	19	Filed pltffs statement concerning those of defts "facts" as to which there are genuine issues.
10-1-75	20	Filed pltffs memo in opposition to intervenor-defts motion for summary judgment.
10-1-75	21	Filed by pltff affdvt of Lorne C.D. MacBeth.
10-15-75	22	Filed Govt's Reply Memo of Law.
12-31-75	23	Filed Opinion #43649. Both motions for summary judgment are denied. Lasker J. (mailed notice)
02-20-76	24	Filed Pltffs. Notice of Change of Attys. Name.

(Continued)

Bristol Lab. Div. of Bristol Myers Co. vs. Staats, U.S.

Lasker J. 75 Civil 1334

DATE	PROCEEDINGS
	Page #3
2-23-76	Filed Dft. & Dft. Intervenor Notice of Deposition of Bristor Lab. Div. etc. on 3-18-76.
07-02-76	Filed deposition of Bristol Laboratories by Richard J. Cormier on 4-6-76. (mailed notice)
10-1-76	Filed Intervenor-deft affidavit and motion ret. 10-22-76.
	Filed govt's memo in support of its motion for summary judgment.
11-5-76	Filed notice of motion for summary judgment ret. 11-15-76 at 10:00 am
11-5-76	Filed memo in support of pltffs renewed motion for summary judgment etc.

DATE	NR.	PROCEEDINGS
11-5-76		Filed Supplemental statement under Rule 9g
11-16-76		Filed govts memo in opposition to pltffs motion for summary judgment.
4-11-77		Filed opinion # 45769 Bristol's motion for summary judgment is granted Govt summary judgment motion is denied Submit judgment on notice Lasker J
7-15-77		Filed Judgment motion for summary judgment of intervenor dft. U.S.A. is denied motion for summary judgment of pltff is granted in all respects, as indicated, counterclaim of USA is dismissed . . . . . Lasker J. Judgment entered 7-15-77 Entered 7-15-77 (mailed notice)
7-18-77		Filed letter to Judge Lasker from U.S.Atty. SDNY dtd. 7-6-77. response & in further support of Comptrollers proposed judgment.
7-18-77		Filed letter to Judge Lasker from U.S. Atty. SDNY dtd. 6-30-77. Re: counter proposed judgment.
7-18-77		Filed Pltffs. Memorandum in opposition to dfts. submission of counter proposed judgment.
9-12-77		Filed intervenor-deft and Elmer B. Staats, Notice of Appeal to the USCA for the 2nd Circuit from the final judgt. entered on 7-15-77.
9-23-77		Filed Pltffs. Notice of Appeal from Judgment dtd. 7-15-77. (mn)
10-21-77		Filed Notice of Certification Record to the USCA.
11-17-77		Filed True Copy of USCA Mandate. Ordered that this action be remanded to the U.S. District Court for the SDNY without prejudice to the pursuance of the appeals from the judgment ent. 7-15-77 etc. (mn)
6/28/79		Filed Copy of Minuete Order pur to Administrative office dtd. 6/15/73, action is statically closed & clerk instructed to submit JS for each case. Orig. filed in 64 Civil 3558-38 (MN)
9-7-79		Fld Consented Protective Order, Lasker J.

BRISTOL LABORATORIES DIVISION OF BRISTOL-MYERS COMPANY, PLAINTIFF-APPELLEE

v.

ELMER B. STAATS, Comptroller General of the United States, DEFENDANT-APPELLANT,

-and-

UNITED STATES OF AMERICA, INTERVENOR-DEFENDANT-APPELLANT

GENERAL DOCKET
UNITED STATES COURT OF APPEALS
FOR THE SECOND CIRCUIT

T-7914

DATE	FILINGS-PROCEEDINGS
	77-6153
9-13-77	Filed copies of docket entries and notice of appeal (USA) (*77-6153*)
9-21-77	Naomi Reice Buchwald, Esq. filed Form C, p/s
9-21-77	Naomi Reice Buchwald, Esq. filed Form D, p/s
9-24-77	Filed copies of notice of appeal and docket entries, (*Bristol Lab. Div.*) (*& in 77-6159*)
10-3-77	Received docket fee (*Bristol Lab*) (*& in 77-6159*)
10-3-77	Weil, Guttman & Davis filed Form C, p/s (& in 77-6159)
10-3-77	Weil, Guttman & Davis filed Form D, p/s (& in 77-6159)
10-5-77	Filed scheduling order #1 (CAMP), PC
10-21-77	Filed record (original papers of district court)
11-7-77	Received stipulation in re: remand to the District Court, etc. (& in 77-6159)
11-14-77	Filed order remanding action to the District Court without prejudice to the pursuance of the appeals from the judgment entered on 7-15-77 after the completion of the proceedings on remand

DATE	FILINGS-PROCEEDINGS
11-15-77	Issued certified copy of order remanding action to the District Court and copy of stipulation in re: remand (& in 77-6159)
11-18-77	Original record returned to district court (& in 77-6159)
12-14-77	Filed receipt of return of original record to district court (& in 77-6159)
12-7-79	Copy of district court "protective order on consent" pursuant to order of USCA dated 11-14-77 remanding action filed. (construed as reinstating appeal pursuant to 11-14-77 order USCA)
12-7-79	Record on appeal filed (Original papers of district court)
12-7-79	Appellant Comptroller General of USA brief, pfs filed
12-7-79	Appellant Comptroller General of USA appendix pfs filed.
12-27-79	Scheduling Order #1, filed.
2-8-80	Appellee Bristol Laboratories Div. brief, pfs filed
2-29-80	Appellant Comptroller General of USA reply brief, pfs filed.
3-10-80	Case argued before Friendly, Feinberg, CJJ, Sifton, D.J.
3-25-80	Judgment affirmed, published opinion, Per Curiam
3-25-80	Judgment filed.
4-24-80	Mandate (Judgment) issued.
8-27-80	Notice of filing of petition for writ of certiorari filed.
12-10-80	Certified copy if order of Supreme Court granting petition for writ of certiorari filed.

UNITED STATES DISTRICT COURT
SOUTHERN DISTRICT OF NEW YORK

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75 Civ. 1334

BRISTOL LABORATORIES DIVISION OF BRISTOL-MYERS COMPANY, PLAINTIFF,

-against-

ELMER B. STAATS, Comptroller General of The United States, DEFENDANT,

-and-

UNITED STATES OF AMERICA, INTERVENOR-DEFENDANT.

MEMORANDUM

APPEARANCES:

WEIL, LEE & BERGIN, ESQS.
60 East 42nd Street
New York, New York 10017
Attorneys for Plaintiff
of Counsel: GILBERT H. WEIL, ESQ.
ROBERT L. SHERMAN, ESQ.

THOMAS J. CAHILL, ESQ.
United States Attorney for the Southern District of New York
One St. Andrew's Plaza
New York, New York 10007
NAOMI REICE BUCHWALD, ESQ.
J. ROGER EDGAR, ESQ.
JOHN G. BROSNAN, ESQ.

LASKER, D.J.

This case involves the scope of the contractual and statutory right of the government to examine certain books and records of the Bristol Laboratories Division of Bristol-Myers Co. (Bristol Labs). Bristol Labs and the

United States, as intervenor-defendant, cross move for summary judgment. The existence of a critical factual question precludes granting judgment for either party.

During 1973 and 1974 Bristol Labs was awarded a number of contracts with the Veterans Administration and the Department of Defense for the sale of pharmaceutical products. Pursuant to 41 U.S.C. § 254(c) each of the contracts included a provision that provides:

> "The Contractor agrees that the Comptroller General of the United States or any of his duly authorized representatives shall, until the expiration of 3 years after final payment under this contract . . . have access to and the right to examine any directly pertinent books, documents, papers, and records of the contractor [or any of its subcontractors] involving the transactions related to this contract."

By letter dated August 26, 1974, Elmer Staats, Comptroller General, informed Bristol Labs that the General Accounting Office was reviewing the procurement of drugs by agencies of the federal government, including the pricing of drugs procured under negotiated contracts. Staats requested pursuant to the contract and to 31 U.S.C. §§ 53, 67; 10 U.S.C. § 2313(b); and 41 U.S.C. § 244(c) that cost records pertinent to the contracts between Bristol and the government be made available for inspection, including:

> "but . . . not limited to (1) records of experienced costs including costs of direct materials, direct labor, overhead, and other pertinent corporate costs, (2) support for prices charged to the Government, and (3) such other information as may be necessary for use to review the reasonableness of the contract prices and the adequacy of the protection afforded the Government's interests." (Exhibit A to the affidavit of Gilbert Weil, submitted in support of plaintiff's motion for summary judgment; Appendix I to affidavit of James Martin, submitted in support of the government's motion for summary judgment.)

This suit arises out of Bristol's unwillingness to allow the government to review records concerning costs incurred

for research and development; marketing and promotion; and distribution and administration.

The documents, affidavits and memoranda of law submitted by the parties establish that the controversy is not as much over the legal construction of the right-of-access clause in the contracts and statutes, as it is a factual dispute concerning Bristol's actual accounting and business procedures.

Bristol does not dispute the government's authority to examine records and verifying data relating to manufacturing costs of the products purchased under the subject contracts and to the establishment of prices for those articles. (Memorandum of law submitted in opposition to the Government's motion for summary judgment, p. 3) Bristol further concedes that the Comptroller General may examine:

> "those records which are directly pertinent to costs incurred in the course of plaintiff's activities related to the supplying of those items purchased under the subject contracts, even though the costs are not assigned by plaintiff to such items." (Memorandum in support of plaintiff's motion for summary judgment, p. 5)

However, Bristol claims that it "does not consider expenses incurred for research and development; advertising and promotion; general and administrative; and distribution . . . in setting contract prices to the Federal Government." (Affidavit of Lorne MacBeth, Vice-President-Marketing, Bristol ¶ 5), and that these records are consequently not subject to governmental examination. Yet, as the government points out, Bristol is inconsistent as to whether costs for those activities are reflected in the price of the products sold to the United States. It notes that Bristol does not, in its Rule 9(g) statement, state that these expenditures are not recovered from *government* revenues, but only that it recovers them

"through revenues generated from sales of its prod-

ucts without allocating them to any customer class, customer or contract."

While the Government agrees with Bristol that the access-to-records clause does not give the Comptroller General access to Bristol's cost records "which are exclusively assigned to or recovered from that firm's non-Government business," (Memorandum of law in support of government's motion for summary judgment, p. 14), the government resists any attempt by Bristol to "frustrate" what it considers to be the legitimate scope of an examination by failing to assign costs, which comprise a portion of the price charged the government, to specific products, and seeks access to Bristol's records as to those costs in order to determine their relationship, if any, to the subject contracts.

Without information as to how these costs are recovered, what Bristol's research and development, and marketing and promotion activities entail, or its method of accounting, it is impossible to determine the correctness of either party's position.

Discovery is necessary to enable the government to inform itself as to Bristol's methods of accounting and allocation of costs. However, Bristol legitimately fears that allowing the Comptroller General to examine its general business records would in essence bring about the opening of its books to the same extent as granting final relief.

We agree with Bristol Labs that the initial discovery to which the Comptroller General is entitled should not be of such scope as to amount to the granting of final relief. Accordingly, both motions for summary judgment are denied. The proper course to follow is to restrict initial discovery by the Comptroller General to deposition of knowledgeable officials of Bristol Labs as to Bristol's methods and procedures for allocation of costs of all items not allocated exclusively to non-government contracts. No discovery shall be made of the books or accounts of Bristol Labs

until termination of the depositions authorized above. Upon termination of such depositions the parties shall be free to move for such relief as appears justified.

The motions are disposed of as indicated above.

It is so ordered.

Dated: New York, New York
December 31, 1975.

MORRIS E. LASKER
U.S.D.J.

UNITED STATES DISTRICT COURT
SOUTHERN DISTRICT OF NEW YORK

Civil Action No.
75 CIV 1334

BRISTOL LABORATORIES DIVISION OF BRISTOL-MYERS COMPANY, PLAINTIFF,

-against-

ELMER B. STAATS, COMPTROLLER GENERAL OF THE UNITED STATES, DEFENDANT.

COMPLAINT FOR DECLARATORY JUDGMENT AND PERMANENT INJUNCTION

Plaintiff, for its complaint herein alleges:

1. Plaintiff Bristol Laboratories is an unincorporated division of Bristol-Myers Company, a Delaware corporation, the principal office of Bristol-Myers Company being in the City of New York, State of New York.

2. The defendant is the Comptroller General of the United States, and, upon information and belief, is not a resident of any state within which plaintiff maintains a principal office.

3. The amount in controversy in the within action exceeds $10,000.00 exclusive of interest and costs.

4. This action arises under the laws of the United States, including the Armed Services Procurement Act, 10 U.S.C. § 2313(b), the Federal Property and Administrative Services Act, 41 U.S.C. § 254(c), and the Administrative Procedure Act, 5 U.S.C. §§ 501 *et seq.*

5. An actual controversy, justiciable in character, exists between the parties hereto with regard to the matters hereinafter set forth.

6. This court has jurisdiction of this action under 28 U.S.C. §§ 1331, 1332, 1337, and 2201-2202, as well as under 5 U.S.C. § 702.

7. During the years 1973 and 1974 plaintiff entered into a number of contracts with the Veterans Administration and with the Department of Defense of the United States for the sale thereto of certain pharmaceutical products.

8. Each of said contracts incorporated within it a provision conferring and delimiting rights of the defendant to have access to and examine certain of plaintiff's records, said agreement being expressed in the following terms:

> "[T]he Comptroller General of the United States or any of his duly authorized representatives shall until the expiration of three years after final payment have access to and the right to examine any directly pertinent books, documents, papers, and records of [Bristol Laboratories] or any of [its] subcontractors engaged in the performance of and involving transactions related to such contracts or subcontracts."

9. Defendant, claiming to be acting pursuant to said contractual provision, is now demanding access to and examination of certain of plaintiff's books, documents, papers, and records, and has threatened that unless plaintiff accedes to such demands defendant "will be required to take such action deemed appropriate to the exercise of our rights under the contracts and the execution of our statutory responsibilities."

10. Plaintiff has, to the contrary, maintained, and alleges, that the items defendant seeks access to and examination of do not constitute books, documents, papers, or records which are directly pertinent to and involve transactions related to the contracts or any subcontracts referred to in paragraphs 7 and 8 above.

11. The items referred to in paragraph 10 above contain highly confidential and sensitive business information and any threat, or weakening or loss of their security will be highly injurious to plaintiff.

12. Without the relief sought herein, defendant's above described unlawful demands, and any overt attempts made

by him to enforce them, will cause plaintiff severe and irreparable injuries, for which it will have no adequate remedy at law.

WHEREFORE, plaintiff prays that this court issue judgment:

1. Declaring that defendant is not entitled to have access to or to examine the books, documents, papers, or records, or any of them, referred to in paragraphs 7 and 8 above; and
2. ordering defendant to specifically conform and confine his examination and attempts to examine plaintiff's books, documents, papers, and records to the terms of the contracts referred to in paragraph 8 above; and
3. enjoining the defendant, temporarily and permanently, and all persons representing him or acting under his direction and authority or acting in concert or participation with him from making any efforts or taking any steps to gain access to or to examine any of said books, documents, papers, or records; and
4. granting such other or further relief as may be appropriate.

Respectfully submitted,
WEIL, LEE & BERGIN

By:/s/_____

Gilbert H. Weil
Attorneys for Plaintiff
Office & P.O. Address
60 East 42nd Street
New York, New York 10017
(212) 687-8573

UNITED STATES DISTRICT COURT
SOUTHERN DISTRICT OF NEW YORK

75 Civ. 1334 (MEL)

BRISTOL LABORATORIES DIVISION OF BRISTOL-MYERS COMPANY, PLAINTIFF,

-against-

ELMER B. STAATS, Comptroller General of The United States, DEFENDANT.

ANSWER

ELMER B. STAATS, Comptroller General of the United States, by his attorney, Paul J. Curran, United States Attorney for the Southern District of New York, for his answer to the Complaint herein alleges as follows:

FIRST: Admits the allegations contained in Paragraph 1 of the Complaint.

SECOND: Admits the allegations contained in Paragraph 2 of the Complaint.

THIRD: Denies the allegations contained in Paragraph 3 of the Complaint.

FOURTH: Denies the allegations contained in Paragraph 4 of the Complaint.

FIFTH: Denies the allegations contained in Paragraph 5 of the Complaint.

SIXTH: Denies the allegations contained in Paragraph 6 of the Complaint.

SEVENTH: Admits the allegations contained in Paragraph 7 of the Complaint.

EIGHTH: Denies the allegations contained in Paragraph 8 of the Complaint.

NINTH: Denies the allegations contained in Paragraph 9 of the Complaint, but admits that a letter dated March 6,

1975 from Elmer B. Staats, Comptroller General of the United States, to Richard L. Gelb, President and Chief Executive Officer of Bristol-Myers Company, contains the words quoted in Paragraph 9 and respectfully refers the Court to that letter for the full contents and meaning thereof.

TENTH: Denies the allegations contained in Paragraph 10 of the Complaint, but respectfully refers the Court to the correspondence and other communications between the parties for the full contents and meaning thereof.

ELEVENTH: Denies having knowledge sufficient to form a belief as to the truth of the allegations contained in Paragraph 11 of the Complaint.

TWELFTH: Denies the allegations contained in Paragraph 12 of the Complaint.

FIRST DEFENSE

THIRTEENTH: The complaint fails to state a claim upon which relief can be granted.

WHEREFORE, defendant respectfully demands that the complaint herein be dismissed and judgment be awarded to the defendant including the costs and disbursements of this action and granting such other relief as the Court may deem appropriate.

Dated: New York, New York
May 19, 1975

PAUL J. CURRAN
United States Attorney
Attorney for Elmer B. Staats,
Comptroller General of the
United States

By: /s/ _____
NAONI REICE BOCHWALD
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Attorney
One St. Andrew's Plaza
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UNITED STATES DISTRICT COURT
SOUTHERN DISTRICT OF NEW YORK

75 Civ. 1334 (MEL)

BRISTOL LABORATORIES DIVISION OF BRISTOL-MYERS COMPANY, PLAINTIFF,

v.

ELMER B. STAATS, Comptroller General of the United States, DEFENDANT

DEFENDANT'S ANSWERS TO PLAINTIFF'S FIRST SET OF INTERROGATORIES

The defendant, Elmer B. Staats, Comptroller General of the United States, by James D. Martin, makes the following answers to written interrogatories served by plaintiff on May 30, 1975.

Plaintiff's Interrogatory No. 1

"1. Identify or describe, as specifically and precisely as possible, each separate book, document, paper or record of the plaintiff to which the defendant claims a right of access and examination."

Answer to Interrogatory No. 1

Defendant does not have knowledge or information sufficient to respond to this interrogatory and accordingly avails itself of the alternative proposed by plaintiff and responds to Interrogatory No. 2.

Plaintiff's Interrogatory No. 2.

"2. If defendant cannot thus identify or describe a par-

ticular book, document, paper or record, then specify it by designing its generic type and nature of subject content."

Answer to Interrogatory No. 2

Defendant maintains that its right of access and examination includes, but is not limited to the following categories of records:

(a) Records relating to those costs assigned by plaintiff to the products purchased under the subject contracts, which industry representatives have indicated are limited essentially to manufacturing costs.

(b) Records relating to those costs which, although they are incurred during the course of plaintiff's activities relating to the supply of ethical pharmaceuticals (including those purchased under subject contracts), are not assigned by the firm to individual products. These costs would include those incurred for activities such as research and development, marketing and promotion, distribution and administration.

(c) Records relating to the methodology, and decisions involved in plaintiff's establishment of prices for the products purchased under the subject contracts.

(d) Records required to verify, to the extent deemed necessary, all data obtained during the course of any review conducted.

However, because of the need to verify all data and because General Accounting Office (GAO) representatives have been provided only very limited access to records by plaintiff, it is not feasible to identify more precisely the specific records needed to be obtained and examined in order to conduct our review.

Plaintiff's Interrogatory No. 3

"3. With respect to each such particular or class of book, document, paper or record identified in response to Interrogatories 1 and 2 above:

A. Name and describe fully:

(1) the specific nature of the transaction or transactions which defendant claims such book, document, paper or record (a) involves and (b) is directly pertinent to; and

(2) the manner and respects in which, and the reasons why, defendant claims each such book, document, paper or record does involve and is directly pertinent to each such transaction.

B. Identify each contract or subcontract to which defendant claims each transaction referred to in Interrogatory 3A(1) relates."

Answer to Interrogatory No. 3

The transactions involved are transactions which relate to the contracts between plaintiff and the Veterans Administration and the Department of Defense, specified in the letter of August 26, 1974, from Elmer B. Staats, Comptroller General of the United States, to Richard Gelb, President and Chief Executive Officer of plaintiff which is annexed hereto as Exhibit A and made a part hereof. Because of the limited access afforded GAO's representatives to the records of the plaintiff, it is not possible to identify the specific transactions to which a particular book, document, paper or record is directly pertinent or with which it is involved.

Beyond the answer herein provided, this interrogatory is objected to on the grounds set forth in the accompanying objections.

Dated: New York, New York

PAUL J. CURRAN
United States Attorney for the
Southern District of New York
Attorney for the United States
of America

By: /s/ _____

NAOMI REICE BUCHWALD
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TO: WEIL, LEE & BERGIN
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CITY OF WASHINGTON)
) ss
DISTRICT OF COLUMBIA)

James D. Martin being duly sworn, deposes and says:

I am, Deputy Director of the Manpower and Welfare Division of the General Accounting Office and have read the interrogatories served upon defendant by plaintiff and the foregoing answers or responses to those interrogatories are true according to the best of my informaton and belief.

/s/ _____
JAMES D. MARTIN

Subscribed and sworn to before me this 27 day of June 1975

/s/ Mary F. Webb
Notary Public

COMPTROLLER GENERAL OF THE
UNITED STATES
WASHINGTON, D.C. 20548

B-146857 August 26, 1974

Mr. Richard L. Gelb
President and Chief Executive Officer
Bristol Laboratories
Division of Bristol-Myers Company
345 Park Avenue
New York, New York 10022

Dear Mr. Gelb:

As you know, because of the increasing Federal involvement in the procurement of pharmaceuticals, the General Accounting Office has underway a review of the procurement of drugs by agencies of the Federal Government, including the pricing of drugs and pharmaceuticals procured under negotiated contracts. This examination is being conducted at several drug companies, including Bristol Laboratories Division, Bristol-Myers Company, and is being made pursuant to the Budget and Accounting Act, 1921 (31 U.S.C. 53), the Accounting and Auditing Act of 1950 (31 U.S.C. 67), and the authority of the Comptroller General to examine contractors' records under the contract provisions pursuant to 10 U.S.C. 2313(b) and 41 U.S.C. 254(c).

For some time we have been attempting to gain access to records we consider necessary to conduct such a review. In this regard, in June 1973 we met with representatives of the Pharmaceutical Manufacturers Association and six drug firms to initiate a comprehensive review using data provided on a voluntary basis by representative industry firms. However, the industry firms have not provided us access to the records necessary to satisfactorily carry out our statutory responsibilities.

On a number of occasions since this effort was initiated, representatives of the drug industry have questioned our right to access to necessary records on the grounds that (1) our request for cost data was considered inappropriate

because the contracts were negotiated on the basis of standard catalog prices without regard to cost or profit margins; (2) the records apply basically to non-Government work; and (3) disclosure of cost data would be of benefit to competitors and damage the company if publicly disclosed. Our Office's right of access to such records was clearly decided by the courts in *Hewlett-Packard Company* v. *United States*, 385 F.2d 1013 (9th Cir. 1967), cert. denied 390 U.S. 988 (1968). The Hewlett-Packard case involved all of the issues the industry has raised.

The purpose of this letter is to formally request that cost records pertinent to contracts listed on enclosure 1 be made available for our examination as provided by the terms of the negotiated contracts awarded to your company by the Defense Supply Agency and the Veterans Administration. We must request that you have the responsible officials at Bristol Laboratories make available to the General Accounting Office as required, all books, documents, papers, and other records directly pertinent to the contracts, which include, but are not limited to (1) records of experienced costs including costs of direct materials, direct labor, overhead, and other pertinent corporate costs, (2) support for prices charged to the Government, and (3) such other information as may be necessary for use to review the reasonableness of the contract prices and the adequacy of the protection afforded the Government's interests. For your information, statements from the legislative history pertaining to the "Examination of Records" clause included in the contracts and our position on the duties and responsibilities that the clause imposes upon my Office are presented in enclosure 2.

We request also that you advise us within 15 days with respect to your decision to make these records available for our examination.

Sincerely yours,

/s/ _____

ELMER B. STAATS
Comptroller General
of the United States

Enclosures—2

LISTING OF CONTRACTS AND, WHERE APPROPRIATE, PURCHASE (DELIVERY) ORDERS TRANSACTED BETWEEN THE U.S. GOVERNMENT AND BRISTOL LABORATORIES

CONTRACT NUMBER	*DATE*
VETERANS ADMINISTRATION:	
V797P-5929b	Mar. 29, 1973
PURCHASE ORDERS:	
74-MC-50116	Sept. 11, 1973
74-MC-50498	Mar. 20, 1974
74-MC-50038	July 26, 1973
74-MC-50490	April 27, 1973
74-MC-50229	Nov. 9, 1973
74-MC-50166	Oct. 15, 1973
74-MC-50153	Sept. 27, 1973
74-MC-50073	Aug. 16, 1973
74-MC-50046	July 31, 1973
74-MC-50341	Jan. 10, 1974
74-MC-50438	Feb. 21, 1974
74-MC-50399	Jan. 29, 1974
74-MC-50307	Dec. 14, 1973
74-MC-50248	Nov. 20, 1973
DEPARTMENT OF DEFENSE:	
DSA120-74-C-2724	Mar. 29, 1974
DSA120-74-C-2404	Feb. 22, 1974
DSA120-73-D-1769	Jan. 22, 1973
DELIVERY ORDERS:	
0001	Jan. 29, 1973
0002	Mar. 16, 1973
0003	Apr. 20, 1973
0005	May 22, 1973
0006	June 15, 1973
0007	July 3, 1973
0008	Aug. 13, 1973
0009	Aug. 30, 1973
0010	Sept. 6, 1973
0011	Oct. 10, 1973

CONTRACT NUMBER	*DATE*
0012	Oct. 25, 1973
0013	Jan. 3, 1974
0014	Jan. 8, 1974
0015	Jan. 15, 1974
0016	Jan. 18, 1974

ENCLOSURE 2

LEGISLATIVE HISTORY AND THE GENERAL ACCOUNTING OFFICE POSITION PERTAINING TO THE EXAMINATION OF RECORDS' CLAUSES

The cited clauses (Clause 10 of the Standard Form 32) were included in the contracts pursuant to Public Law 245, Eighty-second Congress, 65 Stat. 700, which amended section 4 of the Armed Service Procurement Act of 1947 (codified as 10 U.S.C. 2313) and section 304 of the Federal Property and Administrative Services Act of 1949 (codified as 41 U.S.C. 254(c)) by adding the following subsection:

> "(c) All contracts negotiated without advertising pursuant to authority contained in this Act shall include a clause to the effect that the Comptroller General of the United States or any of his duly authorized representatives shall until the expiration of three years after final payment have access to and the right to examine any directly pertinent books, documents, papers, and records of the contractor or any of his subcontractors engaged in the performance of and involving transactions related to such contracts or subcontracts."

Senate Report 603, Eighty-second Congress, to accompany Senate bill 921, which was later enacted as Public Law 245, explained the purpose of the legislation as follows:

> "The Federal Property and Administrative Services Act of 1949 and the Armed Services Procurement Act of 1947 are general legislation of permanent application to a very large percentage of Government procurement. They authorize negotiation of contracts

without advertising under certain specified circumstances in the discretion of the agency head. Since it is well recognized that negotiated contracts are at the same time effective procurement instrumentalities under special circumstances, and require close supervision and control, this legislation would make examination by the Comptroller General a permanent part of procurement procedure on a basis of extending the examination provisions added to the First War Powers Act by Public Law 921 of the Eighty-first Congress."

In considering the legislation, the following statement was made on the floor of the House of Representatives by Congressman Hardy on October 15, 1951 (97 Cong. Rec. 13197):

"This brings up another point. As I have indicated, the authority contained in this bill is really only necessary to cover those cases where the contractors refuse to permit the General Accounting Office to inspect their books and records. As I have already pointed out, the vast majority of contractors do make their books available on a voluntary basis when requested. Thus, this bill would affect that comparative few contractors who now refuse the agent of the Congress permission to see their records. It would be compulsory upon them. It seems logical to me to suppose that there is greater need for the GAO to see the records of those few who do not wish to make them available on a voluntary basis than it is to see the records of those who readily comply. To put it bluntly, those with nothing to hide have nothing to fear by opening their books to the General Accounting Office."

The language of the act and of the legislative history clearly establishes that the statutory provision was enacted to make possible the close supervision and control over negotiated procurements which the Congress regarded as necessary in the interest of the Government. This purpose requires that the act, and the contract provision which is almost identical in language, be interpreted to permit such detailed examination of the contractor's

records to assure the necessary degree of supervision and control. In other words, the clear intent of the statute was to provide for the examination by our Office of such of the contractor's records as would permit a valid evaluation of the reasonableness of the prices charged. This is clearly established by further remarks made by Congressman Hardy on the floor of the House of Representatives immediately after those quoted above (97 Cong. Rec. 13198) as follows:

> "In normal times, competitive bidding generally operates as a brake on the price which a contractor can demand from the Government for his goods and services. However, these are not normal times, and it should be obvious to all of us concerned with the expenditure of billions of dollars for national defense that we must establish every reasonable safeguard against waste and extravagance in the spending of these vast sums. Under conditions as they now exist, competitive bidding has little or no effect upon contracts which are negotiated without advertising. As a result, when a contract is being negotiated, here is a typical illustration of what usually happens: A contractor with years of experience comes to the conference table accompanied by a highly competent accountant and equally competent lawyer. The Government representative on the other side of the table will, in a great majority of cases, be at a tremendous disadvantage, from the standpoint of both training and experience, no matter how conscientious and honest he may be. So, aside from any intentional liberality on the part of the Government contracting officer, there is every chance in the world that the Government will come out on the short end of the deal. *This bill would at least enable the agent of the Congress to check the transactions, both from the Government records and the contractor's books.*" (Emphasis supplied).

The language of the access to records clauses included in the pertinent agreements is modeled closely after the statutory language and was undoubtedly intended to be coextensive in scope. Therefore, we must adhere to the

position stated earlier that under the contracts we are authorized to examine such of the contractor's records as would permit a valid evaluation of the reasonableness of the prices charged without regard to the factors considered or ignored by the contractor in establishing those prices.

Even though other factors are considered in establishing the prices for drugs furnished to the Government and the prices established for may not be directly proportionate to costs, costs of production nevertheless directly pertain to, and involve transactions related to, the contract. Although it is not a condition to the legal authority of the General Accounting Office to have access to such records, we believe that cost records are directly pertinent to the prices established. We believe also that an examination of the relationship of experienced and estimated costs to the prices paid by the Government, and of the pricing methods used in establishing the prices, is clearly within the scope of the type of examination contemplated and required by the terms of the contract.

It is our position, consistent with our interpretation of the act and the contract provision, (1) that all books, documents, papers, and other records relating to the pricing and cost of performance of negotiated contracts are records relating directly to the contracts and to the Government's financial interest, (2) that such books, documents, papers, and other records are not limited to the formal cost accounting records and their supporting data, but include all underlying data concerning contract activities and operations which afford the basis for, or are involved in any way with, the incurrence of costs by the contractor, (3) that the cost records which we requested and other data supporting the prices charged to the Government by the contractor are directly pertinent to the contracts, and (4) that therefore all such books, documents, papers, and other records and underlying data are subject to examination by the General Accounting Office under its statutory responsibility and authority to examine activities and related costs under negotiated contracts.

UNITED STATES DISTRICT COURT
SOUTHERN DISTRICT OF NEW YORK

75 Civ. 1334 (MEL)

BRISTOL LABORATORIES DIVISION OF BRISTOL-MYERS COMPANY, PLAINTIFF

v.

ELMER B. STAATS, Comptroller General of the United States, DEFENDANT

and

UNITED STATES OF AMERICA, INTERVENOR

INTERVENOR'S ANSWER AND COUNTER-CLAIM

The UNITED STATES OF AMERICA, by its attorney, Paul J. Curran, United States Attorney for the Southern District of New York, for its answer to the Complaint herein and its counterclaim alleges as follows:

FIRST: Admits the allegations contained in Paragraph 1 of the Complaint.

SECOND: Admits the allegations contained in Paragraph 2 of the Complaint.

THIRD: Denies the allegations contained in Paragraph 3 of the Complaint.

FOURTH: Denies the allegations contained in Paragraph 4 of the Complaint.

FIFTH: Denies the allegations contained in Paragraph 5 of the Complaint.

SIXTH: Denies the allegations contained in Paragraph 6 of the Complaint.

SEVENTH: Admits the allegations contained in Paragraph 7 of the Complaint.

EIGHTH: Denies the allegations contained in Paragraph

8 of the Complaint.

NINTH: Denies the allegations contained in Paragraph 9 of the Complaint, but admits that a letter dated March 6, 1976 from Elmer B. Staats, Comptroller General of the United States, to Richard E. Gelb, President and Chief Executive Officer of Bristol-Myers Company, contains the words quoted in Paragraph 9 and respectfully refers the Court to that letter for the full contents and meaning thereof.

TENTH: Denies the allegations contained in Paragraph 10 of the Complaint, but respectfully refers the Court to the correspondence and other communications between the parties for the full contents and meaning thereof.

ELEVENTH: Denies having knowledge sufficient to form a belief as to the truth of the allegations contained in Paragraph 11 of the Complaint.

TWELFTH: Denies the allegations contained in Paragraph 12 of the Complaint.

FIRST DEFENSE

THIRTEENTH: The complaint fails to state a claim upon which relief can be granted.

COUNTERCLAIM

FOURTEENTH: This case arises under 10 U.S.C. § 2313(b), 41 U.S.C. § 254(c) and four contracts entered into between the Veterans Administration, Marketing Division, Drug & Chemicals and the Defense Personnel Support Center, Defense Supply Agency and the Bristol Laboratories Division of Bristol-Myers Company (hereinafter referred to as Bristol) pursuant to 10 U.S.C. § 2304(a) and 41 U.S.C. § 252(c).

FIFTEENTH: Jurisdiction is conferred upon this Court by virtue of 28 U.S.C. § 1345 and a request for relief is made pursuant to Title 28 U.S.C. §§ 2201 and 2202.

SIXTEENTH: Plaintiff Bristol is an unincorporated division of Bristol-Myers Company, a corporation organized

and existing under the laws of the State of Delaware, with its principal place of business located in New York, New York.

SEVENTEENTH: On or about March 29, 1973, the Veterans Administration, Marketing Division, Drugs & Chemicals, awarded a contract to plaintiff Bristol which contract was designated as contract number V797P-5929b, wherein Bristol agreed to furnish the Veterans Administration, Marketing Division, Drugs & Chemicals, certain pharmaceutical products. This contract was negotiated pursuant to the provisions of 41 U.S.C. 252(c)(10) and final payment on such contract was made on or about June 25, 1974.

EIGHTEENTH: On or about March 29, 1974, the Defense Personnel Support Center, Defense Supply Agency awarded a contract to plaintiff Bristol which contract was designated as contract number DSA120-74-C-2724, wherein Bristol agreed to furnish to the Defense Personnel Support Center, Defense Supply Agency certain pharmaceutical products. This contract was negotiated pursuant to the provisions of 10 U.S.C. 2304(a)(7) and final payment was made on such contract on or about July 26, 1974.

NINETEENTH: On or about February 26, 1974, the Defense Personnel Support Center, Defense Supply Agency awarded a contract to plaintiff Bristol which contract was designated as contract number DSA120-74-C-2404 wherein Bristol agreed to furnish to the Defense Personnel Support Center, Defense Supply Agency certain pharmaceutical products. This contract was negotiated pursuant to the provisions of 10 U.S.C. 2304(a)(7) and final payment on such contract was made on June 4, 1974.

TWENTIETH: On or about January 23, 1973, the Defense Personnel Support Center, Defense Supply Agency awarded a contract to plaintiff Bristol which contract was designated as contract number DSA120-73-D-1769, wherein Bristol agreed to furnish to the Defense Personnel Support Center, Defense Supply Agency certain pharmaceutical products. This contract was negotiated

pursuant to the provisions of 10 U.S.C. 2304(a)(7) and final payment on such contract was made on June 24, 1974.

TWENTY-FIRST: Each of the aforementioned contracts exceeded the sum of $2,500. Pursuant to the provisions of 41 U.S.C. 254(c) the above-numbered contract mentioned in paragraph SEVENTEENTH of this counterclaim incorporates by reference Veterans Administration Marketing Center Supplemental Provisions No. 1, March 18, 1972, which includes a clause identified as "Examination of Records by Comptroller General" which provides, in part, as follows:

> "(b) The contractor agrees that the Comptroller General of the United States of any of his duly authorized representatives shall, until the expiration of 3 years after final payment under this contract, or such lesser time specified in either Appendix M of the Armed Service Procurement Regulation or the Federal Procurement Regulations Part 1–20, as appropriate, have access to and the right to examine any directly pertinent books, documents, papers, and records of the Contractor involving transactions related to this contract.
>
> "(c) The contractor further agrees to include in all his subcontracts hereinunder a provision to the effect that the subcontractor agrees that the Comptroller General of the United States or any of his duly authorized representatives shall, until the expiration of 3 years after final payment under the subcontract or such lesser time specified in either Appendix M of the Armed Services Procurement Regulation or the Federal Procurement Regulations Part 1–20, as appropriate, have access to and the right to examine any directly pertinent books, documents, papers, and records of such subcontractor involving transactions related to the subcontract. The term 'subcontract' as used in this clause excludes (1) purchase orders not exceeding $2,500 and (2) subcontracts or purchase orders for public utility services at rates established for uniform applicability to the general public."

TWENTY-SECOND: Pursuant to the provisions of 10 U.S.C. § 2313(b) the above-numbered contracts mentioned

in paragraphs EIGHTEENTH and NINETEENTH incorporated by reference Defense Personnel Support Center Master Solicitation (Medical) DPSC Form 3539, January 1973, which incorporates by reference a clause entitled "Examination of Records by Comptroller General" as set forth at Armed Services Procurement Regulation 7–104.15 (1971 ed.). The provisions of this clause are identical to those contained in the clause mentioned in paragraph TWENTY-FIRST of this counterclaim.

TWENTY-THIRD: Pursuant to the provisions of 10 U.S.C. § 2313(b) the above-numbered contract mentioned in paragraph TWENTIETH incorporates by reference Defense Personnel Support Center Master Solicitation, DPSC Form 3385, January 1972, which incorporates by reference a clause entitled "Examination of Records by Comptroller General" as set forth at Armed Services Procurement Regulation 7–104.15 (1971 ed.). The provisions of this clause are identical to those contained in the clause mentioned in paragraph TWENTY-FIRST of this counterclaim.

TWENTY-FOURTH: The contracts mentioned in paragraphs SEVENTEENTH, EIGHTEENTH, NINETEENTH and TWENTIETH of this counterclaim were not entered into by means of formal advertising.

TWENTY-FIFTH: On August 26, 1974, Elmer B. Staats, Comptroller General of the United States, pursuant to the provisions of the clauses denominated "Examination of Records by Comptroller General" mentioned in paragraphs TWENTY-FIRST, TWENTY-SECOND and TWENTY-THIRD of this counterclaim requested from Richard L. Gelb, President and Chief Executive Officer of Bristol, all books, documents, papers, and other records relating to experienced costs including costs of direct materials, labor, overhead, and other corporate costs, support for prices charged to the Government, and such other necessary information which would permit his duly authorized representatives to review the reasonableness of the contract prices provided for in the contracts set forth in this counterclaim.

TWENTY-SIXTH: On September 13, 1974, Douglas R. Purdy, Vice President of Bristol informed the Comptroller General that Bristol would make available to representatives of the Comptroller General "those cost records deemed to be pertinent to said contracts." However, Bristol has refused to honor the Comptroller General's request of August 26.

TWENTY-SEVENTH: Upon information and belief, the books, documents, papers and records relating to the pricing and experienced costs, including costs of direct material, labor, overhead, and other corporate costs hereinbefore mentioned are in the custody and control of the plaintiff Bristol including its officers and subordinates.

TWENTY-EIGHTH: The refusal of the plaintiff to permit the Comptroller General of the United States or his authorized representatives to have access to and to examine the cost data mentioned in paragraph TWENTY-FIFTH of this counterclaim relating to the enumerated contracts in this counterclaim constitutes a violation of the provisions of the "Examination of Records by Comptroller General" clauses included in the contracts pursuant to 10 U.S.C. § 2313(b) and 41 U.S.C. § 254(e) and is in direct contravention of the provisions of clauses contained in the contracts. The refusal to make available for inspection the aforesaid books and records of plaintiff Bristol containing the cost data relating to these contracts have prevented and will continue to prevent the Comptroller General of the United States from discharging his duty and right to examine such books and records and will infringe upon the interest and rights of the United States with respect to the supervision and control of procurement contracts negotiated on behalf of the Federal Government.

TWENTY-NINTH: Intervener has no adequate remedy at law.

WHEREFORE, defendant intervener prays that this court issue an order:

1. Declaring that pursuant to the provisions contained in the contracts designated and referred to in paragraphs

SEVENTEENTH, EIGHTEENTH, NINETEENTH and TWENTIETH of this counterclaim and the provisions of 10 U.S.C. § 2313(b) and 41 U.S.C. § 254(c), the Comptroller General of the United States and his duly authorized representatives have the right to examine all books, documents, papers, or records directly relating to the pricing and cost of producing the items furnished by plaintiff Bristol under the aforesaid contracts, including but not limited to records of experienced costs including costs of direct materials, labor, overhead, and other corporate costs, records in support of prices charged by the plaintiff and all other data and records of Bristol concerning activities and operations of said company which were involved in any way with the incurrence of costs in furnishing the items produced pursuant to said contracts.

2. Enjoining plaintiff Bristol, its officers, agents, servants, attorneys, employees and all persons in active concert or participation with them who receive actual notice of an order by personal service or otherwise, from preventing the duly authorized representatives of the Comptroller General of the United States from obtaining access to and examining any books, documents, papers, or records of the plaintiff that relate to and involve transactions relating to the pricing and cost of producing the items which were furnished by the plaintiff Bristol pursuant to the four contracts enumerated in this counterclaim; and directing plaintiff Bristol including its officers and subordinates at a time and date fixed by the Court to have available on the premises of Bristol Laboratories Division of Bristol-Myers Company, New York, New York, such books and records which the Court adjudges in this action the Comptroller General and his duly authorized representatives have the right to examine.

3. Enjoining plaintiff Bristol acting by and through its officers and subordinates from preventing the duly authorized representatives of the Comptroller General of the United States from obtaining access to and examining any books, documents, papers, or records of plaintiff that relate to and involve transactions relating to pricing and ex-

perienced costs including costs of direct materials, labor, overhead and other corporate costs, support for prices charged to the Government and such other necessary information which would permit his representatives to review the reasonableness of the contract prices provided for in the aforesaid contracts.

4. Dismissing the complaint and granting such other and further relief as may be just and equitable.

Dated: New York, New York
July 3, 1975.

Respectfully submitted,

PAUL J. CURRAN
United States Attorney for the Southern District of New York
Attorney for the United States of America

By: /s/_____
NAOMI REICE BUCHWALD
Assistant United States Attorney
Office & Post Office Address:
One St. Andrew's Plaza
New York, New York 10007
Telephone: (212) 791-1972

UNITED STATES DISTRICT COURT
SOUTHERN DISTRICT OF NEW YORK

Civil Action No.
75 CIV 1334 (MEL)

BRISTOL LABORATORIES DIVISION OF
BRISTOL-MYERS COMPANY, PLAINTIFF,

-against-

ELMER B. STAATS, COMPTROLLER GENERAL
OF THE UNITED STATES, DEFENDANT,

and

UNITED STATES OF AMERICA, INTERVENOR-DEFENDANT.

REPLY TO COUNTERCLAIM

Plaintiff, for its reply to intervenor-defendant's counterclaim, states as follows:

1. Admits the allegations of paragraph Fourteenth of intervenor-defendant's counterclaim to the extent that the action arises under 10 U.S.C. § 2313(b) and 41 U.S.C. § 254(c) and that plaintiff entered into contracts with the Defense Personnel Support Center and independently thereof entered into a contract with the Veterans Administration.

2. Denies that this Court has jurisdiction under 28 U.S.C. § 1345, as alleged in paragraph Fifteenth of intervenor-defendant's counterclaim, but admits that this Court has jurisdiction under 28 U.S.C. §§ 1331, 1332, 1337, 2201, 2202 and 5 U.S.C. § 702.

3. Admits the allegations of paragraph Sixteenth of intervenor-defendant's counterclaim.

4. Admits the allegations of paragraph Seventeenth of intervenor-defendant's counterclaim.

5. Admits the allegations of paragraph Eighteenth of intervenor-defendant's counterclaim.

6. Admits the allegations of paragraph Nineteenth of intervenor-defendant's counterclaim, except that contract number DSA 120-74-C-2404 was entered into on or about February 22, 1974.

7. Admits the allegations of paragraph Twentieth of intervenor-defendant's counterclaim, except that contract number DSA 120-73-D-1769 was entered into on or about January 22, 1973.

8. Admits the allegations of paragraph Twenty-first of intervenor-defendant's counterclaim.

9. Admits the allegations of paragraph Twenty-second of intervenor-defendant's counterclaim.

10. Admits the allegations of paragraph Twenty-third of intervenor-defendant's counterclaim.

11. Admits the allegations of paragraph Twenty-fourth of intervenor-defendant's counterclaim.

12. Denies the allegations of paragraph Twenty-fifth of intervenor-defendant's counterclaim, but admits that a letter sent under date of August 26, 1974 from Elmer B. Staats to Richard L. Gelb, President and Chief Executive Officer of plaintiff, which letter is attached hereto as Exhibit 1 and is self-explanatory of its content.

13. Admits the allegations of the first sentence of paragraph Twenty-sixth of intervenor-defendant's counterclaim. Denies the allegations of the second sentence of said paragraph and relies on the letter dated March 18, 1975, from plaintiff's counsel to defendant Staats, attached as Exhibit 2 hereto.

14. Admits that it has records of certain costs but otherwise denies the allegations of paragraph Twenty-seventh of intervenor-defendant's counterclaim.

15. Denies the allegations of paragraph Twenty-eighth of intervenor-defendant's counterclaim.

16. Denies the allegations of paragraph Twenty-ninth of intervenor-defendant's counterclaim.

AS AND FOR A SEPARATE DEFENSE

17. Intervenor-defendant's counterclaim fails to state a claim upon which relief may be granted.

WHEREFORE, plaintiff prays that this Court issue an order dismissing intervenor-defendant's counterclaim and granting such other and further relief as may be just.

Respectfully submitted,

WEIL, LEE & BERGIN

By /s/ _____

GILBERT H. WEIL
Attorneys for Plaintiff
Office and P.O. Address
60 East 42nd Street
New York, New York 10017
(212) 687-8573

COMPTROLLER GENERAL OF THE
UNITED STATES
WASHINGTON, D.C. 20548

B-146857 August 26, 1974

Mr. Richard L. Gelb
President and Chief Executive Officer
Bristol Laboratories
Division of Bristol-Myers Company
345 Park Avenue
New York, New York 10022

Dear Mr. Gelb:

As you know, because of the increasing Federal involvement in the procurement of pharmaceuticals, the General Accounting Office has underway a review of the procurement of drugs by agencies of the Federal Government, including the pricing of drugs and pharmaceuticals procured under negotiated contracts. This examination is being conducted at several drug companies, including Bristol Laboratories Division, Bristol-Myers Company, and is being made pursuant to the Budget and Accounting Act, 1921 (31 U.S.C. 53), the Accounting and Auditing Act of 1950 (31 U.S.C. 67), and the authority of the Comptroller General to examine contractors' records under the contract provisions pursuant to 10 U.S.C. 2313(b) and 41 U.S.C. 254(c).

For some time we have been attempting to gain access to records we consider necessary to conduct such a review. In this regard, in June 1973 we met with representatives of the Pharmaceutical Manufacturers Association and six drug firms to initiate a comprehensive review using data provided on a voluntary basis by representative industry firms. However, the industry firms have not provided us access to the records necessary to satisfactorily carry out our statutory responsibilities.

On a number of occasions since this effort was initiated, representatives of the drug industry have questioned our right to access to necessary records on the grounds that (1) our request for cost data was considered inappropriate

because the contracts were negotiated on the basis of standard catalog prices without regard to cost or profit margins; (2) the records apply basically to non-Government work; and (3) disclosure of cost data would be of benefit to competitors and damage the company if publicly disclosed. Our Office's right of access to such records was clearly decided by the courts in *Hewlett-Packard Company* v. *United States*, 385 F.2d 1013 (9th Cir. 1967), cert. denied 390 U.S. 988 (1968). The Hewlett-Packard case involved all of the issues the industry has raised.

The purpose of this letter is to formally request that cost records pertinent to contracts listed on enclosure 1 be made available for our examination as provided by the terms of the negotiated contracts awarded to your company by the Defense Supply Agency and the Veterans Administration. We must request that you have the responsible officials at Bristol Laboratories make available to the General Accounting Office as required, all books, documents, papers, and other records directly pertinent to the contracts, which include, but are not limited to (1) records of experienced costs including costs of direct materials, direct labor, overhead, and other pertinent corporate costs, (2) support for prices charged to the Government, and (3) such other information as may be necessary for use to review the reasonableness of the contract prices and the adequacy of the protection afforded the Government's interests. For your information, statements from the legislative history pertaining to the "Examination of Records" clause included in the contracts and our position on the duties and responsibilities that the clause imposes upon my Office are presented in enclosure 2.

We request also that you advise us within 15 days with respect to your decision to make these records available for our examination.

Sincerely yours,

/s/ _____

ELMER B. STAATS
Comptroller General of the United States

Enclosures—2

LISTING OF CONTRACTS AND, WHERE APPROPRIATE, PURCHASE (DELIVERY) ORDERS TRANSACTED BETWEEN THE U.S. GOVERNMENT AND BRISTOL LABORATORIES

CONTRACT NUMBER	*DATE*
VETERANS ADMINISTRATION:	
V797P-5929b	Mar. 29, 1973
PURCHASE ORDERS:	
74-MC-50116	Sept. 11, 1973
74-MC-50498	Mar. 20, 1974
74-MC-50038	July 26, 1973
74-MC-50490	April 27, 1973
74-MC-50229	Nov. 9, 1973
74-MC-50166	Oct. 15, 1973
74-MC-50153	Sept. 27, 1973
74-MC-50073	Aug. 16, 1973
74-MC-50046	July 31, 1973
74-MC-50341	Jan. 10, 1974
74-MC-50438	Feb. 21, 1974
74-MC-50399	Jan. 29, 1974
74-MC-50307	Dec. 14, 1973
74-MC-50248	Nov. 20, 1973
DEPARTMENT OF DEFENSE:	
DSA120-74-C-2724	Mar. 29, 1974
DSA120-74-C-2404	Feb. 22, 1974
DSA120-73-D-1769	Jan. 22, 1973
DELIVERY ORDERS:	
0001	Jan. 29, 1973
0002	Mar. 16, 1973
0003	Apr. 20, 1973
0005	May 22, 1973
0006	June 15, 1973
0007	July 3, 1973
0008	Aug. 13, 1973
0009	Aug. 30, 1973
0010	Sept. 6, 1973
0011	Oct. 10, 1973
0012	Oct. 25, 1973

CONTRACT NUMBER	*DATE*
0013	Jan. 3, 1974
0014	Jan. 8, 1974
0015	Jan. 15, 1974
0016	Jan. 18, 1974

ENCLOSURE 2

LEGISLATIVE HISTORY AND THE GENERAL ACCOUNTING OFFICE POSITION PERTAINING TO THE EXAMINATION OF RECORDS' CLAUSES

The cited clauses (Clause 10 of the Standard Form 32) were included in the contracts pursuant to Public Law 245, Eighty-second Congress, 65 Stat. 700, which amended section 4 of the Armed Service Procurement Act of 1947 (codified as 10 U.S.C. 2313) and section 304 of the Federal Property and Administrative Services Act of 1949 (codified as 41 U.S.C. 254(c)) by adding the following subsection:

> "(c) All contracts negotiated without advertising pursuant to authority contained in this Act shall include a clause to the effect that the Comptroller General of the United States or any of his duly authorized representatives shall until the expiration of three years after final payment have access to and the right to examine any directly pertinent books, documents, papers, and records of the contractor or any of his subcontractors engaged in the performance of and involving transactions related to such contracts or subcontracts."

Senate Report 603, Eighty-second Congress, to accompany Senate bill 921, which was later enacted as Public Law 245, explained the purpose of the legislation as follows:

> "The Federal Property and Administrative Services Act of 1949 and the Armed Services Procurement Act of 1947 are general legislation of permanent application to a very large percentage of Government procurement. They authorize negotiation of contracts without advertising under certain specified circumstances in the discretion of the agency head. Since it

> is well recognized that negotiated contracts are at the same time effective procurement instrumentalities under special circumstances, and require close supervision and control, this legislation would make examination by the Comptroller General a permanent part of procurement procedure on a basis of extending the examination provisions added to the First War Powers Act by Public Law 921 of the Eighty-first Congress."

In considering the legislation, the following statement was made on the floor of the House of Representatives by Congressman Hardy on October 15, 1951 (97 Cong. Rec. 13197):

> "This brings up another point. As I have indicated, the authority contained in this bill is really only necessary to cover those cases where the contractors refuse to permit the General Accounting Office to inspect their books and records. As I have already pointed out, the vast majority of contractors do make their books available on a voluntary basis when requested. Thus, this bill would affect that comparative few contractors who now refuse the agent of the Congress permission to see their records. It would be compulsory upon them. It seems logical to me to suppose that there is greater need for the GAO to see the records of those few who do not wish to make them available on a voluntary basis than it is to see the records of those who readily comply. To put it bluntly, those with nothing to hide have nothing to fear by opening their books to the General Accounting Office."

The language of the act and of the legislative history clearly establishes that the statutory provision was enacted to make possible the close supervision and control over negotiated procurements which the Congress regarded as necessary in the interest of the Government. This purpose requires that the act, and the contract provision which is almost identical in language, be interpreted to permit such detailed examination of the contractor's records to assure the necessary degree of supervision and control. In other words, the clear intent of the statute was

to provide for the examination by our Office of such of the contractor's records as would permit a valid evaluation of the reasonableness of the prices charged. This is clearly established by further remarks made by Congressman Hardy on the floor of the House of Representatives immediately after those quoted above (97 Cong. Rec. 13198) as follows:

> "In normal times, competitive bidding generally operates as a brake on the price which a contractor can demand from the Government for his goods and services. However, these are not normal times, and it should be obvous to all of us concerned with the expenditure of billions of dollars for national defense that we must establish every reasonable safeguard against waste and extravagance in the spending of these vast sums. Under conditions as they now exist, competitive bidding has little or no effect upon contracts which are negotiated without advertising. As a result, when a contract is being negotiated, here is a typical illustration of what usually happens: A contractor with years of experience comes to the conference table accompanied by a highly competent accountant and equally competent lawyer. The Government representative on the other side of the table will, in a great majority of cases, be at a tremendous disadvantage, from the standpoint of both training and experience, no matter how conscientious and honest he may be. So, aside from any intentional liberality on the part of the Government contracting officer, there is every chance in the world that the Government will come out on the short end of the deal. *This bill would at least enable the agent of the Congress to check the transactions, both from the Government records and the contractor's books.*" (Emphasis supplied.)

The language of the access to records clauses included in the pertinent agreements is modeled closely after the statutory language and was undoubtedly intended to be coextensive in scope. Therefore, we must adhere to the position stated earlier that under the contracts we are authorized to examine such of the contractor's records as

would permit a valid evaluation of the reasonableness of the prices charged without regard to the factors considered or ignored by the contractor in establishing those prices.

Even though other factors are considered in establishing the prices for drugs furnished to the Government and the prices established for may not be directly proportionate to costs, costs of production nevertheless directly pertain to, and involve transactions related to, the contract. Although it is not a condition to the legal authority of the General Accounting Office to have access to such records, we believe that cost records are directly pertinent to the prices established. We believe also that an examination of the relationship of experienced and estimated costs to the prices paid by the Government, and of the pricing methods used in establishing the prices, is clearly within the scope of the type of examination contemplated and required by the terms of the contract.

It is our position, consistent with our interpretation of the act and the contract provision, (1) that all books, documents, papers, and other records relating to the pricing and cost of performance of negotiated contracts are records relating directly to the contracts and to the Government's financial interest, (2) that such books, documents, papers, and other records, are not limited to the formal cost accounting records and their supporting data, but include all underlying data concerning contract activities and operations which afford the basis for, or are involved in any way with, the incurrence of costs by the contractor, (3) that the cost records which we requested and other data supporting the prices charged to the Government by the contractor are directly pertinent to the contracts, and (4) that therefore all such books, documents, papers, and other records and underlying data are subject to examination by the General Accounting Office under its statutory responsibility and authority to examine activities and related costs under negotiated contracts.

March 18, 1975

Hon. Elmer B. Staats
Comptroller General of the
United States
Washington, D.C. 20548

Re: *Your #B-146857*

Dear Sir:

On behalf of our client, Bristol-Myers Company, we wish to thank you for the opportunity extended by your letter of March 6, 1975 to Mr. Richard L. Gelb to restate clearly our client's position, and its rationale, respecting your request referred to in that letter.

We do not, nor have we ever, disputed your rights of access and examination under our contracts to all books, documents, papers, and records that are *directly* pertinent to and involve those transactions which determined the prices set in such contracts (please see our letters to you of September 13, 1974 and to Mr. Gregory J. Ahart of November 18, 1974).

Conversely, in our opinion books, documents, papers, or records pertinent to and involving transactions which established the prices in *other* contracts with *other* persons, but which do not take place and were not operant factors with respect to the contracts you have listed are not pertinent to, and do not involve transactions relating to such contracts.

It is, therefore, our position that the terms of our contracts protect such books, documents, papers, and records against access and examination.

Having little doubt that you disagree with Bristol-Myers' decision, we believe it best that the matter be judicially resolved as expeditiously as possible. We, therefore enclose a courtesy copy of a complaint we are filing this

day in the District Court for the Southern District of New York.

RESPECTFULLY YOURS,

GHW
GHW:rb
Enclosure

UNITED STATES DISTRICT COURT
SOUTHERN DISTRICT OF NEW YORK

Civil Action No. 75 CIV 1334 (MEL)

BRISTOL LABORATORIES DIVISION OF BRISTOL-MYERS COMPANY, PLAINTIFF,

-against-

ELMER B. STAATS, COMPTROLLER GENERAL OF THE UNITED STATES, DEFENDANT,

AND

UNITED STATES OF AMERICA, INTERVENOR-DEFENDANT.

NOTICE OF MOTION FOR SUMMARY JUDGMENT PURSUANT TO RULE 56, F.R.C.P.

SIRS:

PLEASE TAKE NOTICE that, upon the annexed statement of material facts as to which there is no genuine issue to be tried, the accompanying affidavit of Gilbert H. Weil, dated July 22, 1975, the pleadings herein, defendant Staats' answers to plaintiff's first set of interrogatories and the accompanying memorandum, plaintiff will move this Court at room 2903, United States Courthouse, Foley Square, New York, New York, on the 1st day of August, 1975 at 10:00 o'clock in the forenoon, for an order that plaintiff is entitled to judgment as a matter of law (1) limiting defendant Staats' access to and examination of plaintiff's books, documents, papers and records, in accordance with 10 U.S.C. § 2313(b) and 41 U.S.C. § 254(c) and various contracts between plaintiff and the United States, to those records which are directly pertinent to and involve transactions related to such contracts, (2) prohibiting defendant Staats from gaining access to and conducting an examination of plaintiff's books, documents, papers or rec-

ords which are pertinent to and involve transactions related only to contracts other than the aforesaid contracts and (3) dismissing intervenor-defendant's counterclaim except to the extent that it properly seeks access to and examination of those of plaintiff's books, documents, papers and records which are directly pertinent to and involve transactions related to the said government contracts.

GROUNDS FOR MOTION

1. Within the past three years, plaintiff entered into a number of contracts with the United States for the sale of certain pharmaceutical products. Each of those contracts contained a provision permitting defendant Staats to examine such records of plaintiff as are directly pertinent to and involve transactions related to such contracts. Defendant Staats has insisted on access to and examination of records of plaintiff that pertain to and involve transactions related only to contracts other than those with the United States.

2. Intervenor-defendant has filed a counterclaim asking that plaintiff be enjoined from refusing to give access to and to permit examination of those of its records demanded by defendant Staats. Such counterclaim has no legal basis under contract or statutory law insofar as it requires plaintiff to produce records that are not directly pertinent to and do not involve transactions related to the subject contracts.

Yours, etc.
WEIL, LEE & BERGIN

By _____

GILBERT H. WEIL
Attorneys for Plaintiff
Office and P.O. Address
60 East 42nd Street
New York, New York 10017
(212) 687-8573

TO: NAOMI REICE BUCHWALD
Assistant U. S. Attorney
U. S. Courthouse Annex
Room 526
One St. Andrews Plaza
New York, New York 10007

UNITED STATES DISTRICT COURT
SOUTHERN DISTRICT OF NEW YORK

Civil Action No.
75 CIV 1334 (MEL)

BRISTOL LABORATORIES DIVISION OF
BRISTOL-MYERS COMPANY, PLAINTIFF,

-against-

ELMER B. STAATS, COMPTROLLER GENERAL OF
THE UNITED STATES, DEFENDANT,

AND

UNITED STATES OF AMERICA, INTERVENOR-DEFENDANT.

STATEMENT UNDER LOCAL RULE 9(g)

STATEMENT OF THE MATERIAL FACTS AS TO WHICH THERE ARE NO GENUINE ISSUES

The following is a statement of the material facts as to which plaintiff contends there is no genuine issue to be tried.

1. On or about January 22, 1973, plaintiff entered into a contract with the Defense Personnel Support Center, Defense Supply Agency, for the sale of certain pharmaceutical products. Said contract is identified as DSA 120-73-D-1769.

2. On or about March 29, 1973, plaintiff entered into a contract with the Veterans Administration, Marketing Division, Drugs & Chemicals, for the sale of certain pharmaceutical products. Said contract is identified as V797P-5929b.

3. On or about February 22, 1974, plaintiff entered into a contract with the Defense Personnel Support Center, Defense Supply Agency, for the sale of certain pharmaceutical products. Said contract is identified as DSA 120-74-C-2404.

4. On or about March 29, 1974, plaintiff entered into a contract with the Defense Personnel Support Center, Defense Supply Agency, for the sale of certain pharmaceutical products. Said contract is identified as DSA 120-74-C-2724.

5. Each of the aforementioned contracts had incorporated therein a clause that provided, in part:

> "(b) The Contractor agrees that the Comptroller General of the United States or any of his duly authorized representatives shall, until the expiration of 3 years after final payment under this contract or such lesser time specified in either Appendix M of the Armed Services Procurement Regulation or the Federal Procurement Regulations Part 1-20, as appropriate, have access to and the right to examine any directly pertinent books, documents, papers, and records of the Contractor involving transactions related to this contract.
>
> "(c) The Contractor further agrees to include in all his subcontracts hereunder a provision to the effect that the subcontractor agrees that the Comptroller General of the United States or any of his duly authorized representatives shall, until the expiration of 3 years after final payment under the subcontract of such lesser time specified in either Appendix M of the Armed Services Procurement Regulation or the Federal Procurement Regulations Part 1-20, as appropriate, have access to and the right to examine any directly pertinent books, documents, papers, and records of such subcontractor, involving transactions related to the subcontract. The term "subcontract" as used in this clause excludes (i) purchase orders not exceeding $2,500 (ii) subcontracts or purchase orders for public utility services at rates established for uniform applicability to the general public."

6. The aforementioned contracts were not entered into by means of formal advertising.

7. In a letter dated August 26, 1974 from defendant Staats to Mr. Richard L. Gelb, President and Chief Executive Officer of plaintiff, defendant formally requested that plaintiff make available for examination by defendant all records of costs directly pertinent to the subject contracts, but did not limit his request to records of expenses incurred for the items sold under those contracts. Exhibit A to moving (Weil) affidavit.

8. By letter dated September 13, 1974, from Douglas R. Purdy, Vice-President of plaintiff, to defendant Staats, plaintiff agreed to make available at its Syracuse office those cost records deemed to be pertinent to the subject contracts. Weil aff't, Exh.B.

9. In a letter dated November 18, 1974, from Mr. Purdy to Gregory J. Ahart, Director, Manpower and Welfare Division, United States General Accounting Office, plaintiff agreed to make available in February 1975, for examination by defendant Staats' representatives, those of its records that are directly pertinent to the subject contracts. Weil aff't, Exh. C.

10. On or about February 10 and 11, 1975, representatives of defendant Staats met with representatives of plaintiff in the latter's offices in Syracuse, New York. Although plaintiff made available for examination by defendant Staats' representatives those records it felt are directly pertinent to the subject contracts, said records were deemed incomplete by defendant Staats' representatives.

11. Under date of March 6, 1975, defendant Staats, in a letter to Mr. Richard L. Gelb, informed plaintiff that if it did not comply within 10 days with his formal request of August 26th, he would take "such action deemed appropriate." Weil aff't, Exh. D.

12. By letter of March 18, 1975, Gilbert H. Weil, counsel to plaintiff, restated plaintiff's position of willingness to

comply with its statutory and contractual obligations. Weil aff't, Exh. E.

Yours, etc.
WEIL, LEE & BERGIN
By /s/_____
GILBERT H. WEIL
Attorneys for Plaintiff
Office and P.O. Address
60 East 42nd Street
New York, New York 10017
(212) 687-6573

UNITED STATES DISTRICT COURT
SOUTHERN DISTRICT OF NEW YORK

Civil Action No. 75 CIV 1334 (MEL)

BRISTOL LABORATORIES DIVISION OF
BRISTOL-MYERS COMPANY, PLAINTIFF,

-against-

ELMER B. STAATS, COMPTROLLER GENERAL
OF THE UNITED STATES, DEFENDANT,

AND

UNITED STATES OF AMERICA,
INTERVENOR-DEFENDANT.

AFFIDAVIT

STATE OF NEW YORK)
) ss.:
COUNTY OF NEW YORK)

GILBERT H. WEIL, being duly sworn, deposes as follows:

1. I am a member of the bar of this Court and, as counsel for the plaintiff Bristol Laboratories Division of Bristol-Myers Company, make this affidavit in support of said plaintiff's motion for summary judgment.

2. The purpose of this affidavit is to bring before the court the following exhibits annexed hereto:

Exhibit A. A letter of August 26, 1974, from defendant Staats to Mr. Richard L. Gelb, President and Chief Executive Officer of plaintiff, formally requesting plaintiff to make available all records directly pertinent to the subject contracts, but not limiting said request to expenses incurred for the items sold under those contracts.

Exhibit B. A letter of September 13, 1974, from Mr. Douglas R. Purdy, Vice-President of plaintiff, to defendant Staats, indicating plaintiff's willingness to make available for examination those cost records deemed to be pertinent to the subject contracts.

Exhibit C. A letter of November 18, 1974, from Mr. Purdy to Mr. Gregory J. Ahart, Director, Manpower and Welfare Division, United States General Accounting Office, agreeing to a meeting at plaintiff's offices in Syracuse, New York for the examination by defendant Staats' representatives of those of plaintiff's records that are directly pertinent to the subject contracts.

Exhibit D. A letter of March 6, 1975, from defendant Staats to Richard L. Gelb, threatening to take "appropriate" action against plaintiff if it did not comply with the formal request of August 26th.

Exhibit E. A letter of March 18, 1975, from affiant, as counsel to plaintiff, to defendant Staats, restating plaintiff's position of willingness to comply with the statutes and the contracts.

Exhibit F. A copy of defendant Staats' answers to plaintiff's first set of interrogatories, preceded in each instance by plaintiff's request.

3. Exhibits A, B, C and D, above, are submitted on information and belief, affiant having no direct knowledge thereof, beyond plaintiff's representations to him.

4. The effect of these exhibits is, as will be more fully described in plaintiff's accompanying memorandum in support of its motion for summary judgment, to show the court that there are no issues of fact raised by plaintiff's said motion.

5. The foregoing exhibits, especially D, E and F, set forth the history and the focus of the controversy herein.

6. The sole issue raised by the within motion, namely, the determination of the scope of the statutes and contracts granting to defendant Staats the right of access to and examination of those of plaintiff's records which are

directly pertinent to and involve transactions related to the subject contracts, is a question of law.

/s/ _____
GILBERT H. WEIL

Sworn to before me this 22nd day of July 1975.

/s/ _____
Notary Public

COMPTROLLER GENERAL OF THE
UNITED STATES
WASHINGTON, D.C. 20548

B-146857 August 26, 1974

Mr. Richard L. Gelb
President and Chief Executive Officer
Bristol Laboratories
Division of Bristol-Myers Company
345 Park Avenue
New York, New York 10022

Dear Mr. Gelb:

As you know, because of the increasing Federal involvement in the procurement of pharmaceuticals, the General Accounting Office has underway a review of the procurement of drugs by agencies of the Federal Government, including the pricing of drugs and pharmaceuticals procured under negotiated contracts. This examination is being conducted at several drug companies, including Bristol Laboratories Division, Bristol-Myers Company, and is being made pursuant to the Budget and Accounting Act, 1921 (31 U.S.C. 53), the Accounting and Auditing Act of 1950 (31 U.S.C. 67), and the authority of the Comptroller General to examine contractors' records under the contract provisions pursuant to 10 U.S.C. 2313(b) and 41 U.S.C. 254(c).

For some time we have been attempting to gain access to records we consider necessary to conduct such a review. In this regard, in June 1973 we met with representatives of the Pharmaceutical Manufacturers Association and six drug firms to initiate a comprehensive review using data provided on a voluntary basis by representative industry firms. However, the industry firms have not provided us access to the records necessary to satisfactorily carry out our statutory responsibilities.

On a number of occasions since this effort was initiated, representatives of the drug industry have questioned our

EXHIBIT A

right to access to necessary records on the grounds that (1) our request for cost data was considered inappropriate because the contracts were negotiated on the basis of standard catalog prices without regard to cost or profit margins; (2) the records apply basically to non-Government work; and (3) disclosure of cost data would be of benefit to competitors and damage the company if publicly disclosed. Our Office's right of access to such records was clearly decided by the courts in *Hewlett-Packard Company* v. *United States*, 385 F.2d 1013 (9th Cir. 1967), cert. denied 390 U.S. 988 (1968). The Hewlett-Packard case involved all of the issues the industry has raised.

The purpose of this letter is to formally request that cost records pertinent to contracts listed on enclosure 1 be made available for our examination as provided by the terms of the negotiated contracts awarded to your company by the Defense Supply Agency and the Veterans Administration. We must request that you have the responsible officials at Bristol Laboratories make available to the General Accounting Office as required, all books, documents, papers, and other records directly pertinent to the contracts, which include, but are not limited to (1) records of experienced costs including costs of direct materials, direct labor, overhead, and other pertinent corporate costs, (2) support for prices charged to the Government, and (3) such other information as may be necessary for use to review the reasonableness of the contract prices and the adequacy of the protection afforded the Government's interests. For your information, statements from the legislative history pertaining to the "Examination of Records" clause included in the contracts and our position on the duties and responsibilities that the clause imposes upon my Office are presented in enclosure 2.

We request also that you advise us within 15 days with respect to your decision to make these records available for our examination.

Sincerely yours,

/s/ _____

ELMER B. STAATS
Comptroller General
of the United States

Enclosures—2

ENCLOSURE 1

LISTING OF CONTRACTS
AND, WHERE APPROPRIATE,
PURCHASE (DELIVERY) ORDERS
TRANSACTED BETWEEN THE
U.S. GOVERNMENT AND BRISTOL LABORATORIES

CONTRACT NUMBER	*DATE*
VETERANS ADMINISTRATION:	
V797P-5929b	Mar. 29, 1973
PURCHASE ORDERS:	
74-MC-50116	Sept. 11, 1973
74-MC-50498	Mar. 20, 1974
74-MC-50038	July 26, 1973
74-MC-50490	April 27, 1973
74-MC-50229	Nov. 9, 1973
74-MC-50166	Oct. 15, 1973
74-MC-50153	Sept. 27, 1973
74-MC-50073	Aug. 16, 1973
74-MC-50046	July 31, 1973
74-MC-50341	Jan. 10, 1974
74-MC-50438	Feb. 21, 1974
74-MC-50399	Jan. 29, 1974
74-MC-50307	Dec. 14, 1973
74-MC-50248	Nov. 20, 1973
DEPARTMENT OF DEFENSE:	
DSA120-74-C-2724	Mar. 29, 1974
DSA120-74-C-2404	Feb. 22, 1974
DSA120-73-D-1769	Jan. 22, 1973
DELIVERY ORDERS:	
0001	Jan. 29, 1973
0002	Mar. 16, 1973
0003	Apr. 20, 1973
0005	May 22, 1973
0006	June 15, 1973
0007	July 3, 1973
0008	Aug. 13, 1973
0009	Aug. 30, 1973
0010	Sept. 6, 1973
0011	Oct. 10, 1973

CONTRACT NUMBER	*DATE*
DELIVERY ORDERS:	
0012	Oct. 25, 1973
0013	Jan. 3, 1974
0014	Jan. 8, 1974
0015	Jan. 15, 1974
0016	Jan. 18, 1974

ENCLOSURE 2

LEGISLATIVE HISTORY AND THE GENERAL ACCOUNTING OFFICE POSITION PERTAINING TO THE EXAMINATION OF RECORDS' CLAUSES

The cited clauses (Clause 10 of the Standard Form 32) were included in the contracts pursuant to Public Law 245, Eighty-second Congress, 65 Stat. 700, which amended section 4 of the Armed Service Procurement Act of 1947 (codified as 10 U.S.C. 2313) and section 304 of the Federal Property and Administrative Services Act of 1949 (codified as 41 U.S.C. 254(c)) by adding the following subsection:

> "(c) All contracts negotiated without advertising pursuant to authority contained in this Act shall include a clause to the effect that the Comptroller General of the United States or any of his duly authorized representatives shall until the expiration of three years after final payment have access to and the right to examine any directly pertinent books, documents, papers, and records of the contractor or any of his subcontractors engaged in the performance of and involving transactions related to such contracts or subcontracts."

Senate Report 603, Eighty-second Congress, to accompany Senate bill 921, which was later enacted as Public Law 245, explained the purpose of the legislation as follows:

> "The Federal Property and Administrative Services Act of 1949 and the Armed Services Procurement Act of 1947 are general legislation of permanent application to a very large percentage of Government

procurement. They authorize negotiation of contracts without advertising under certain specified circumstances in the discretion of the agency head. Since it is well recognized that negotiated contracts are at the same time effective procurement instrumentalities under special circumstances, and require close supervision and control, this legislation would make examination by the Comptroller General a permanent part of procurement procedure on a basis of extending the examination provisions added to the First War Powers Act by Public Law 921 of the Eighty-first Congress."

In considering the legislation, the following statement was made on the floor of the House of Representatives by Congressman Hardy on October 15, 1951 (97 Cong. Rec 13197):

"This brings up another point. As I have indicated, the authority contained in this bill is really only necessary to cover those cases where the contractors refuse to permit the General Accounting Office to inspect their books and records. As I have already pointed out, the vast majority of contractors do make their books available on a voluntary basis when requested. Thus, this bill would affect that comparative few contractors who now refuse the agent of the Congress permission to see their records. It would be compulsory upon them. It seems logical to me to suppose that there is greater need for the GAO to see the records of those few who do not wish to make them available on a voluntary basis than it is to see the records of those who readily comply. To put it bluntly, those with nothing to hide have nothing to fear by opening their books to the General Accounting Office."

The language of the act and of the legislative history clearly establishes that the statutory provision was enacted to make possible the close supervision and control over negotiated procurements which the Congress regarded as necessary in the interest of the Government. This purpose requires that the act, and the contract provision which is almost identical in language, be interpreted to permit such detailed examination of the contractor's

records to assure the necessary degree of supervision and control. In other words, the clear intent of the statute was to provide for the examination by our Office of such of the contractor's records as would permit a valid evaluation of the reasonableness of the prices charged. This is clearly established by further remarks made by Congressman Hardy on the floor of the House of Representatives immediately after those quoted above (97 Cong. Rec. 13198) as follows:

> "In normal times, competitive bidding generally operates as a brake on the price which a contractor can demand from the Government for his goods and services. However, these are not normal times, and it should be obvious to all of us concerned with the expenditure of billions of dollars for national defense that we must establish every reasonable safeguard against waste and extravagance in the spending of these vast sums. Under conditions as they now exist, competitive bidding has little or no effect upon contracts which are negotiated without advertising. As a result, when a contract is being negotiated, here is a typical illustration of what usually happens: A contractor with years of experience comes to the conference table accompanied by a highly competent accountant and equally competent lawyer. The Government representative on the other side of the table will, in a great majority of cases, be at a tremendous disadvantage, from the standpoint of both training and experience, no matter how conscientious and honest he may be. So, aside from any intentional liberality on the part of the Government contracting officer, there is every chance in the world that the Government will come out on the short end of the deal. *This bill would at least enable the agent of the Congress to check the transactions, both from the Government records and the contractor's books.*" (Emphasis supplied.)

The language of the access to records clauses included in the pertinent agreements is modeled closely after the statutory language and was undoubtedly intended to be coextensive in scope. Therefore, we must adhere to the position stated earlier that under the contracts we are au-

thorized to examine such of the contractor's records as would permit a valid evaluation of the reasonableness of the prices charged without regard to the factors considered or ignored by the contractor in establishing those prices.

Even though other factors are considered in establishing the prices for drugs furnished to the Government and the prices established for may not be directly proportionate to costs, costs of production nevertheless directly pertain to, and involve transactions related to, the contract. Although it is not a condition to the legal authority of the General Accounting Office to have access to such records, we believe that cost records are directly pertinent to the prices established. We believe also that an examination of the relationship of experienced and estimated costs to the prices paid by the Government, and of the pricing methods used in establishing the prices, is clearly within the scope of the type of examination contemplated and required by the terms of the contract.

It is our position, consistent with our interpretation of the act and the contract provision, (1) that all books, documents, papers, and other records relating to the pricing and cost of performance of negotiated contracts are records relating directly to the contracts and to the Government's financial interest, (2) that such books, documents, papers, and other records are not limited to the formal cost accounting records and their supporting data, but include all underlying data concerning contract activities and operations which afford the basis for, or are involved in any way with, the incurrence of costs by the contractor, (3) that the cost records which we requested and other data supporting the prices charged to the Government by the contractor are directly pertinent to the contracts, and (4) that therefore all such books, documents, papers, and other records and underlying data are subject to examination by the General Accounting Office under its statutory responsibility and authority to examine activities and related costs under negotiated contracts.

BRISTOL LABORATORIES
DIVISION OF BRISTOL-MYERS COMPANY
SYRACUSE, NEW YORK 13201

D. R. PURDY
VICE PRESIDENT

September 13, 1974

Mr. Elmer B. Staats
Comptroller General of the United States
United States General Accounting Office
Washington, D.C. 20548

Dear Mr. Staats:

This letter is in reply to the letter, dated August 26, 1974, from you to Mr. Richard L. Gelb, President of Bristol-Myers Company, requesting formally that Bristol Laboratories Division make available for examination certain cost records pertinent to contracts listed on Enclosure I of your letter.

We wish to advise that it is agreeable to the Company to make available for examination at our Syracuse office those cost records deemed to be pertinent to said contracts. However, prior to any visit of your staff to Syracuse for this purpose, we respectfully request an opportunity to meet and discuss with you or your representatives the methods and procedures to be followed in connection with such examination. As I related to Mr. Gregory J. Ahart, Director Manpower & Welfare Division, in my letter of June 7, 1974, our staff is rather limited at the present time and we seek to arrange for the smooth conduct of the examination.

We will be available at your convenience for such a meeting and we look forward to hearing from you or your representative in this regard.

VERY TRULY YOURS,

/s/ _____

DOUGLAS R. PURDY
Vice President
Bristol Laboratories Division

DRP:lb

EXHIBIT B

November 18, 1974

Mr. Gregory J. Ahart
Director
Manpower and Welfare Division
United States General Accounting Office
Washington, D.C. 20548

Dear Greg:

I should like to confirm what I explained to you over the telephone today. We have given serious consideration to your proposal for a "Phase II" type study of the pharmaceutical industry and have concluded that we will not participate in such an effort. Although some mutual benefit might have resulted from our involvement, we believe that it would have entailed considerable effort on our part at a time when our staff is stretched very thin. Furthermore, we believe that it would involve access to details of our business which are truly confidential, and you have made it clear that you cannot guarantee that confidentiality would be maintained.

As I stated in my letter to Mr. Staats, dated September 13, 1974, we are agreeable to an examination of cost records deemed pertinent to the contracts enumerated in his letter of August 26 to Mr. Gelb, President of Bristol-Myers Company. You are aware that we are, at this time, involved with audits by the Internal Revenue Service, the Customs Bureau and our external auditors—Messrs. Price, Waterhouses and Company. We wish to cooperate with you, but you can appreciate the strain which all of these projects place upon our organization.

In order to best facilitate the work of your auditors as well as to minimize confusion for my staff I should like to suggest that your examination commence after our year-end closing—say about February 1.

EXHIBIT C

Of course, if you wish to meet before that date to discuss procedures and scope, I am sure that can be arranged.

VERY TRULY YOURS,
/s/ _____
D. R. PURDY

DRP:lb

COMPTROLLER GENERAL OF
THE UNITED STATES
WASHINGTON, D.C. 20548

B-146857 March 6, 1975

Mr. Richard L. Gelb
President and Chief Executive Officer
Bristol-Myers Company
345 Park Avenue
New York, New York 10022

Dear Mr. Gelb:

In a letter dated August 26, 1974, I formally requested that Bristol Laboratories Division of Bristol-Myers Company make available to our Office for examination all books, documents, papers and other records pertinent to several specified Government contracts.

Following additional contacts between your firm and our Office, Mr. D. R. Purdy, Vice President, Bristol Laboratories Division, in a letter dated November 18, 1974, informed Mr. Gregory J. Ahart, Director of our Manpower and Welfare Division, that your firm was agreeable to an examination of cost records deemed pertinent to the contracts cited in my letter of August 26, 1974. Mr. Purdy requested that our examination begin about February 1, 1975, and arrangements were made for our examination to begin on February 10, 1975.

On February 10 and 11, 1975, representatives of our Office met with Mr. Purdy and other Bristol representatives in Syracuse, New York, to begin the examination of records. During this visit, the Bristol representatives stated that the firm was willing to make available for our examination and vertification, (1) Bristol's contract files which included shipment and invoice records, (2) records and data relating to manufacturing costs assigned by the firm to the products purchased under the contracts, and (3) Bristol's product prices to its non-Federal customers.

EXHIBIT D

The representatives stated, however, that Bristol was unwilling to make available for our review, records concerning costs incurred for activities such as research and development, marketing and promotion, distribution and administration. According to the representatives, such costs are not assigned to individual products and records concerning these costs are not pertinent to the cited contracts. The representatives stated also that Bristol did not consider as pertinent to the contracts, records relating to the methodology and decisions involved in the firm's establishment of prices for the products purchased under the contracts.

We believe that your firm's position regarding our request for access to records pertinent to specified contracts does not meet the requirements of the statutes under which our request was made. In addition, we believe that in the absence of access to the data which your firm is not presently inclined to provide us, we cannot appropriately meet our statutory responsibilities to the Congress.

We therefore have concluded that in the absence of access to such data, we must interpret your firm's actions as a refusal of our formal request for access to records pertinent to the cited contracts. If you believe that we have misinterpreted your firm's position, we request that you so inform us within 10 days and advise us of the date when it would be convenient for us to commence our review of your firm's records.

In the absence of a response from your firm indicating that we have misinterpreted your firm's position concerning this matter, we will be required to take such action deemed appropriate to the exercise of our rights under the contracts and the execution of our statutory responsibilities.

Sincerely yours,

/s/ _____

ELMER B. STAATS
Comptroller General
of the United States

March 18, 1975

Hon. Elmer B. Staats
Comptroller General of the
United States
Washington, D. C. 20548

Re: *Your #B-146857*

Dear Sir:

On behalf of our client, Bristol-Myers Company, we wish to thank you for the opportunity extended by your letter of March 6, 1975 to Mr. Richard L. Gelb to restate clearly our client's position, and its rationale, respecting your request referred to in that letter.

We do not, nor have we ever, disputed your rights of access and examination under our contracts to all books, documents, papers, and records that are *directly* pertinent to and involve those transactions which determined the prices set in such contracts (please see our letters to you of September 13, 1974 and to Mr. Gregory J. Ahart of November 18, 1974).

Conversely, in our opinion books, documents, papers, or records pertinent to and involving transactions which established the prices in *other* contracts with *other* persons, but which did not take place and were not operant factors with respect to the contracts you have listed are not pertinent to, and do not involve transactions relating to such contracts.

It is, therefore, our position that the terms of our contracts protect such books, documents, papers, and records against access and examination.

Having little doubt that you disagree with Bristol-Myers' decision, we believe it best that the matter be judicially resolved as expeditiously as possible. We, therefore, enclose a courtesy copy of a complaint we are filing this day in the District Court for the Southern District of New York.

Respectfully yours,

GHW:rb
Enclosure

EXHIBIT E

UNITED STATES DISTRICT COURT
SOUTHERN DISTRICT OF NEW YORK

75 Civ. 1334 (MEL)

BRISTOL LABORATORIES DIVISION OF BRISTOL-MEYERS COMPANY, PLAINTIFF,

-*v*-

ELMER B. STAATS, COMPTROLLER GENERAL OF THE UNITED STATES, DEFENDANT.

DEFENDANT'S ANSWERS TO PLAINTIFF'S FIRST SET OF INTERROGATORIES

The defendant, Elmer B. Staats, Comptroller General of the United States, by James D. Martin, makes the following answers to written interrogatories served by plaintiff on May 30, 1975.

Plaintiff's Interrogatory No. 1

"1. Identify or describe, as specifically and precisely as possible, each separate book, document, paper or record of the plaintiff to which the defendant claims a right of access and examination."

Answer to Interrogatory No. 1

Defendant does not have knowledge or information sufficient to respond to this interrogatory and accordingly avails itself of the alternative proposed by plaintiff and responds to Interrogatory No. 2.

Plaintiff's Interrogatory No. 2

"2. If defendant cannot thus identify or describe a particular book, document, paper or record, then specify it by

designating its generic type and nature of subject content."

Answer to Interrogatory No. 2

Defendant maintains that its right of access and examination includes, but is not limited to the following categories of records:

(a) Records relating to those costs assigned by plaintiff to the products purchased under the subject contracts, which industry representatives have indicated are limited essentially to manufacturing costs.

(b) Records relating to those costs which, although they are incurred during the course of plaintiff's activities relating to the supply of ethical pharmaceuticals (including those purchased under subject contracts), are not assigned by the firm to individual products. These costs would include those incurred for activities such as research and development, marketing and promotion, distribution and administration.

(c) Records relating to the methodology, and decisions involved in plaintiff's establishment of prices for the products purchased under the subject contracts.

(d) Records required to verify, to the extent deemed necessary, all data obtained during the course of any review conducted.

However, because of the need to verify all data and because General Accounting Office (GAO) representatives have been provided only very limited access to records by plaintiff, it is not feasible to identify more precisely the specific records needed to be obtained and examined in order to conduct our review.

Plaintiff's Interrogatory No. 3

"3. With respect to each such particular or class of book, document, paper or record identified in response to Interrogatories 1 and 2 above:

A. Name and describe fully:

(1) the specific nature of the transaction or transactions which defendant claims such book, document, paper or record (a) involves and (b) is directly pertinent to; and

(2) the manner and respects in which, and the reasons why, defendant claims each such book, document, paper or record does involve and is directly pertinent to each such transaction.

B. Identify each contract or subcontract to which defendant claims each transaction referred to in Interrogatory 3A(1) relates."

Answer to Interrogatory No. 3

The transactions involved are transactions which relate to the contracts between plaintiff and the Veterans Administration and the Department of Defense, specified in the letter of August 26, 1974, from Elmer B. Staats, Comptroller General of the United States, to Richard Gelb, President and Chief Executive Officer of Plaintiff which is annexed hereto as Exhibit A and made a part hereof. Because of the limited access afforded GAO's representatives to the records of the plaintiff, it is not possible to identify the specific transactions to which a particular book, document, paper or record is directly pertinent or with which it is involved.

Beyond the answer herein provided, this interrogatory is objected to on the grounds set forth in the accompanying objections.

Dated: New York, New York

PAUL J. CURRAN
United States Attorney for the
Southern District of New York
Attorney for the
United States of America

By: /s/_____
NAOMI REICE BUCHWALD
Assistant United States Attorney
Office & Post Office Address:
One St. Andrew's Plaza
New York, New York 10007
Telephone: (212) 791-1972

TO: WEIL, LEE & BERGIN
Attorneys for Plaintiff
Office and P. O. Address
60 East 42nd Street
New York, New York 10017
Telephone: (212) 687-8573

CITY OF WASHINGTON)
) ss
DISTRICT OF COLUMBIA)

James D. Martin being duly sworn, deposes and says:

I am, Deputy Director of the Manpower and Welfare Division of the General Accounting Office and have read the interrogatories served upon defendant by plaintiff and the foregoing answers or responses to those interrogatories are true according to the best of my information and belief.

/s/ _____
JAMES D. MARTIN

Subscribed and sworn to before me this 27 day of June 1975

/s/ Mary F. Webb
Notary Public

COMPTROLLER GENERAL OF THE
UNITED STATES
WASHINGTON, D.C. 20548

B-146857 August 26, 1974

Mr. Richard L. Gelb
President and Chief Executive Officer
Bristol Laboratories
Division of Bristol-Myers Company
345 Park Avenue
New York, New York 10022

Dear Mr. Gelb:

As you know, because of the increasing Federal involvement in the procurement of pharmaceuticals, the General Accounting Office has underway a review of the procurement of drugs by agencies of the Federal Government, including the pricing of drugs and pharmaceuticals procured under negotiated contracts. This examination is being conducted at several drug companies, including Bristol Laboratories Division, Bristol-Myers Company, and is being made pursuant to the Budget and Accounting Act, 1921 (31 U.S.C. 53), the Accounting and Auditing Act of 1950 (31 U.S.C. 67), and the authority of the Comptroller General to examine contractors' records under the contract provisions pursuant to 10 U.S.C. 2313(b) and 41 U.S.C. 254(c).

For some time we have been attempting to gain access to records we consider necessary to conduct such a review. In this regard, in June 1973 we met with representatives of the Pharmaceutical Manufacturers Association and six drug firms to initiate a comprehensive review using data provided on a voluntary basis by representative industry firms. However, the industry firms have not provided us

access to the records necessary to satisfactorily carry out our statutory responsibilities.

On a number of occasions since this effort was initiated, representatives of the drug industry have questioned our right to access to necessary records on the grounds that (1) our request for cost data was considered inappropriate because the contracts were negotiated on the basis of standard catalog prices without regard to cost or profit margins; (2) the records apply basically to non-Government work; and (3) disclosure of cost data would be of benefit to competitiors and damage the company if publicly disclosed. Our Office's right of access to such records was clearly decided by the courts in *Hewlett-Packard Company* v. *United States*, 385 F.2d 1013 (9th Cir. 1967), cert. denied 390 U.S. 988 (1968). The Hewlett-Packard case involved all of the issues the industry has raised.

The purpose of this letter is to formally request that cost records pertinent to contracts listed on enclosure 1 be made available for our examination as provided by the terms of the negotiated contracts awarded to your company by the Defense Supply Agency and the Veterans Administration. We must request that you have the responsible officials at Bristol Laboratories make available to the General Accounting Office as required, all books, documents, papers, and other records directly pertinent to the contracts, which include, but are not limited to (1) records of experienced costs including costs of direct materials, direct labor, overhead, and other pertinent corporate costs, (2) support for prices charged to the Government, and (3) such other information as may be necessary for use to review the reasonableness of the contract prices and the adequacy of the protection afforded the Government's interests. For your information, statements from the legislative history pertaining to the "Examination of Records" clause included in the contracts and our position on the duties and responsibilities that the clause imposes upon my Office are presented in enclosure 2.

We request also that you advise us within 15 days with

respect to your decision to make these records available for our examination.

Sincerely yours,

/s/ _____

ELMER B. STAATS
Comptroller General
of the United States

Enclosures—2

LISTING OF CONTRACTS AND, WHERE APPROPRIATE, PURCHASE (DELIVERY) ORDERS TRANSACTED BETWEEN THE U.S. GOVERNMENT AND BRISTOL LABORATORIES

CONTRACT NUMBER	*DATE*
VETERANS ADMINISTRATION:	
V797P-5929b	Mar. 29, 1973
PURCHASE ORDERS:	
74-MC-50116	Sept. 11, 1973
74-MC-50498	Mar. 20, 1974
74-MC-50038	July 26, 1973
74-MC-50490	April 27, 1973
74-MC-50229	Nov. 9, 1973
74-MC-50166	Oct. 15, 1973
74-MC-50153	Sept. 27, 1973
74-MC-50073	Aug. 16, 1973
74-MC-50046	July 31, 1973
74-MC-50341	Jan. 10, 1974
74-MC-50438	Feb. 21, 1974
74-MC-50399	Jan. 29, 1974
74-MC-50307	Dec. 14, 1973
74-MC-50243	Nov. 20, 1973
DEPARTMENT OF DEFENSE:	
DSA120-74-C-2724	Mar. 29, 1974
DSA120-74-C-2404	Feb. 22, 1974
DSA120-73-D-1769	Jan. 22, 1973
DELIVERY ORDERS:	
0001	Jan. 29, 1973
0002	Mar. 16, 1973
0003	Apr. 20, 1973
0005	May 22, 1973
0006	June 15, 1973
0007	July 3, 1973
0008	Aug. 13, 1973
0009	Aug. 30, 1973
0010	Sept. 6, 1973

CONTRACT NUMBER	*DATE*
DELIVERY ORDERS:	
0011	Oct. 10, 1973
0012	Oct. 25, 1973
0013	Jan. 3, 1974
0014	Jan. 8, 1974
0015	Jan. 15, 1974
0016	Jan. 18, 1974

ENCLOSURE 2

LEGISLATIVE HISTORY AND THE GENERAL ACCOUNTING OFFICE POSITION PERTAINING TO THE EXAMINATION OF RECORDS' CLAUSES

The cited clauses (Clause 10 of the Standard Form 32) were included in the contracts pursuant to Public Law 245, Eighty-second Congress, 65 Stat. 700, which amended section 4 of the Armed Service Procurement Act of 1947 (codified as 10 U.S.C. 2313) and section 304 of the Federal Property and Administrative Services Act of 1949 (codified as 41 U.S.C. 254(c)) by adding the following subsection:

> "(c) All contracts negotiated without advertising pursuant to authority contained in this Act shall include a clause to the effect that the Comptroller General of the United States or any of his duly authorized representatives shall until the expiration of three years after final payment have access to and the right to examine any directly pertinent books, documents, papers, and records of the contractor or any of his subcontractors engaged in the performance of and involving transactions related to such contracts or subcontracts."

Senate Report 603, Eighty-second Congress, to accompany Senate bill 921, which was later enacted as Public Law 245, explained the purpose of the legislation as follows:

> "The Federal Property and Administrative Services Act of 1949 and the Armed Services Procurement

> Act of 1947 are general legislation of permanent application to a very large percentage of Government procurement. They authorize negotiation of contracts without advertising under certain specified circumstances in the discretion of the agency head. Since it is well recognized that negotiated contracts are at the same time effective procurement instrumentalities under special circumstances, and require close supervision and control, this legislation would make examination by the Comptroller General a permanent part of procurement procedure on a basis of extending the examination provisions added to the First War Powers Act by Public Law 921 of the Eighty-first Congress."

In considering the legislation, the following statement was made on the floor of the House of Representatives by Congressman Hardy on October 15, 1951 (97 Cong. Rec. 13197):

> "This brings up another point. As I have indicated, the authority contained in this bill is really only necessary to cover those cases where the contractors refuse to permit the General Accounting Office to inspect their books and records. As I have already pointed out, the vast majority of contractors do make their books available on a voluntary basis when requested. Thus, this bill would affect that comparative few contractors who now refuse the agent of the Congress permission to see their records. It would be compulsory upon them. It seems logical to me to suppose that there is greater need for the GAO to see the records of those few who do not wish to make them available on a voluntary basis than it is to see the records of those who readily comply. To put it bluntly, those with nothing to hide have nothing to fear by opening their books to the General Accounting Office."

The language of the act and of the legislative history clearly establishes that the statutory provision was enacted to make possible the close supervision and control over negotiated procurements which the Congress regarded as necessary in the interest of the Government. This purpose requires that the act, and the contract provi-

sion which is almost identical in language, be interpreted to permit such detailed examination of the contractor's records to assure the necessary degree of supervision and control. In other words, the clear intent of the statute was to provide for the examination by our Office of such of the contractor's records as would permit a valid evaluation of the reasonableness of the prices charged. This is clearly established by further remarks made by Congressman Hardy on the floor of the House of Representatives immediately after those quoted above (97 Cong. Rec. 13198) as follows:

> "In normal times, competitive bidding generally operates as a brake on the price which a contractor can demand from the Government for his goods and services. However, these are not normal times, and it should be obvious to all of us concerned with the expenditure of billions of dollars for national defense that we must establish every reasonable safeguard against waste and extravagance in the spending of these vast sums. Under conditions as they now exist, competitive bidding has little or no effect upon contracts which are negotiated without advertising. As a result, when a contract is being negotiated, here is a typical illustration of what usually happens: A contractor with years of experience comes to the conference table accompanied by a highly competent accountant and equally competent lawyer. The Government representative on the other side of the table will, in a great majority of cases, be at a tremendous disadvantage, from the standpoint of both training and experience, no matter how conscientious and honest he may be. So, aside from any intentional liberality on the part of the Government contracting officer, there is every chance in the world that the Government will come out on the short end of the deal. *This bill would at least enable the agent of the Congress to check the transactions, both from the Government records and the contractor's books.*" (Emphasis supplied.)

The language of the access to records clauses included in the pertinent agreements is modeled closely after the statutory language and was undoubtedly intended to be

coextensive in scope. Therefore, we must adhere to the position stated earlier that under the contracts we are authorized to examine such of the contractor's records as would permit a valid evaluation of the reasonableness of the prices charged without regard to the factors considered or ignored by the contractor in establishing those prices.

Even though other factors are considered in establishing the prices for drugs furnished to the Government and the prices established for may not be directly proportionate to costs, costs of production nevertheless directly pertain to, and involve transactions related to, the contract. Although it is not a condition to the legal authority of the General Accounting Office to have access to such records, we believe that cost records are directly pertinent to the prices established. We believe also that an examination of the relationship of experienced and estimated costs to the prices paid by the Government, and of the pricing methods used in establishing the prices, is clearly within the scope of the type of examination contemplated and required by the terms of the contract.

It is our position, consistent with our interpretation of the act and the contract provision, (1) that all books, documents, papers, and other records relating to the pricing and cost of performance of negotiated contracts are records relating directly to the contracts and to the Government's financial interest, (2) that such books, documents, papers, and other records are not limited to the formal cost accounting records and their supporting data, but include all underlying data concerning contract activities and operations which afford the basis for, or are involved in any way with, the incurrence of costs by the contractor, (3) that the cost records which we requested and other data supporting the prices charged to the Government by the contractor are directly pertinent to the contracts, and (4) that therefore all such books, documents, papers, and other records and underlying data are subject to examination by the General Accounting Office under its statutory responsibility and authority to examine activities and related costs under negotiated contracts.

UNITED STATES DISTRICT COURT
SOUTHERN DISTRICT OF NEW YORK

75 Civ. 1334 (MEL)

BRISTOL LABORATORIES DIVISION OF BRISTOL-MYERS COMPANY, PLAINTIFF,

-against-

ELMER B. STAATS, COMPTROLLER GENERAL OF THE UNITED STATES, DEFENDANT.

DEFENDANT'S OBJECTIONS TO PLAINTIFF'S FIRST SET OF INTERROGATORIES

Defendant Elmer B. Staats, Comptroller General of the United States, objects to Interrogatory Number 3 of the Interrogatories served upon him by plaintiff on the 30th day of May, 1975 on the ground that the interrogatory, except to the extent that defendant has responded thereto, requests information not within the knowledge of possession of the defendant but within the sole knowledge and possession of the plaintiff.

Dated: New York, New York
June 30, 1975

PAUL J. CURRAN
United States Attorney for the
Southern District of New York
Attorney for the Defendant

/s/ _____

NAOMI REICE BUCHWALD
Assistant United States Attorney
Office and Post Office Address:
United States Courthouse Annex
One St. Andrew's Plaza
New York, New York 10007
Telephone: (212) 791-1972

To:
WEIL, LEE & BERGIN
Attorney for Plaintiff
60 East 42nd Street
New York, New York 10017

UNITED STATES DISTRICT COURT
SOUTHERN DISTRICT OF NEW YORK

75 Civ. 1334 (MEL)

BRISTOL LABORATORIES DIVISION OF BRISTOL-MYERS COMPANY, PLAINTIFF,

-against-

ELMER B. STAATS, COMPTROLLER GENERAL OF THE UNITED STATES, DEFENDANT,

and

UNITED STATES OF AMERICA,
INTERVENOR-DEFENDANT.

NOTICE OF MOTION

SIRS:

PLEASE TAKE NOTICE that upon the pleadings, the affidavit of John G. Brosnan, Esq., sworn to on August 21, 1975 and annexed as Exhibit A, the affidavit of James D. Martin, sworn to on August 21, 1975, and annexed as Exhibit B, the affidavit of Paul G. Dembling, Esq., sworn to August 25, 1975 and the Rule 9(g) Statement annexed as Exhibit C, and upon all prior proceedings had herein, the intervenor-defendant, United States of America, will move before the Honorable Morris E. Lasker, on September 10, 1975 at 10:00 in the forenoon of that day in Room 2903, United States Courthouse, Foley Square, New York, New York, for an order pursuant to Rule 56 of the Federal Rules of Civil Procedure awarding summary judgment to the United States for the relief prayed for in its counterclaim on the ground that there is no genuine issue as to any material fact and that the United States is entitled to judgment as a matter of law and for such other and further relief as the Court deems to be proper.

Dated: New York, New York
August 28, 1975

PAUL J. CURRAN
United States Attorney for the
Southern District of New York
Attorney for Defendants

By: /s/ _____
NAOMI REICE BUCHWALD
Assistant United States
Attorney

Office and Post Office Address:
United States Courthouse Annex
One St. Andrew's Plaza
New York, New York 10007

To: WEIL, LEE & BERGIN, ESQS.
60 East 42 Street
New York, New York 10017

UNITED STATES DISTRICT COURT
SOUTHERN DISTRICT OF NEW YORK

75 Civ. 1334 (MEL)

BRISTOL LABORATORIES DIVISION OF BRISTOL-MYERS COMPANY, PLAINTIFF,

v

ELMER B. STAATS, COMPTROLLER GENERAL OF THE UNITED STATES, DEFENDANT.

AFFIDAVIT OF JOHN G. BROSNAN
IN SUPPORT OF MOTION OF THE UNITED STATES
FOR SUMMARY JUDGMENT

CITY OF WASHINGTON)
) ss
DISTRICT OF COLUMBIA)

John G. Brosnan being first duly sworn, deposes and says:

1. In the course of my duties as an attorney-advisor with the General Accounting Office I had occasion to review contract numbers V797P-5929b, DSA120-74-C-2404, DSA120-74-C-2724, DSA120-73-D-1769, which form the subject matter of the present suit.

Contract V797P-5929b

2. With respect to contract number V797P-5929b, I determined the following: this contract was awarded to Bristol Laboratories Division of Bristol-Myers Company (Bristol) by the Veterans Administration, Marketing Division, Drugs & Chemicals (VA) on or about March 29, 1973. This requirements type contract was executed to cover the needs of VA for several different pharmaceutical products

from April 1, 1973 through March 31, 1974 at an estimated price of $684,682.68. This contract was negotiated by VA pursuant to the authority of 41 U.S.C. 252(c) (10) and sections 1-3.210(a) (1) and (2) of the Federal Procurement Regulations (FPR) (1964 ed.). 41 U.S.C. 252(c) (10) provides that contracts may be negotiated without formal advertising if "for property or services for which it is impracticable to obtain competition." FPR 1-3.210(a) (1) (1964 ed.) provides that the negotiation authority of 41 U.S.C. 252(c) (10) may be invoked if the property or services can be obtained from only one source or firm. FPR 1-3.210(a) (2) (1964 ed.) provides that such authority may be invoked when competition is precluded because of the existence of patent rights, copyrights, secret processes, control of basic raw material or similar circumstances. Final payment on this contract was made on or about June 25, 1974.

Pursuant to the provisions of 41 U.S.C. 254(c) the above named contract incorporates by reference Veterans Administration Marketing Center Supplemental Provisions No. 1, March 18, 1972, which includes a clause identified as "Examination of Records by Comptroller General" which provides as follows:

> *"EXAMINATION OF RECORDS BY COMPTROLLER GENERAL*
>
> (a) This clause is applicable if the amount of this contract exceeds $2,500 and was entered into by means of negotiation, including small business restricted advertising, but is not applicable if this contract was entered into by means of formal advertising.
>
> (b) The Contractor agrees that the Comptroller General of the United States or any of his duly authorized representatives shall, until the expiration of 3 years after final payment under this contract or such lesser time specified in either Appendix M of the Armed Services Procurement Regulation or the Federal Procurement Regulations Part 1-20, as appropriate, have access to and the right to examine any directly pertinent books, documents, papers, and rec-

ords of the Contractor involving transactions related to this contract.

(c) The Contractor further agrees to include in all his subcontracts hereunder a provision to the effect that the subcontractor agrees that the Comptroller General of the United States or any of his duly authorized representatives shall, until the expiration of 3 years after final payment under the subcontract or such lesser time specified in either Appendix M of the Armed Services Procurement Regulation or the Federal Procurement Regulation Part 1-20, as appropriate, have access to and the right to examine any directly pertinent books, documents, papers and records of such subcontractor, involving transactions related to the subcontract. The term 'subcontract' as used in this clause excludes (1) purchase orders not exceeding $2,500 and (2) subcontracts or purchase orders for public utility services at rates established for uniform applicability to the general public.

(d) The periods of access and examination described in (b) and (c), above, for records which relate to (1) appeals under the 'Disputes' clause of this contract, (2) litigation or the settlement of claims arising out of the performance of this contract, (3) costs and expenses of this contract, as to which exception has been taken by the Comptroller General or any of his duly authorized representatives, shall continue until such appeals, litigation, claims or exceptions have been disposed of."

Contract DSA120-74-C-2404

3. With respect to contract number DSA120-74-C-2404, I determined the following: this contract was awarded to Bristol by the Defense Personnel Support Center, Defense Supply Agency (DSA) on or about February 26, 1974 for a definite quantity of Ampicillin capsules at a price of $34,649.19. This contract was negotiated by DSA pursuant to the authority of 10 U.S.C. 2304(a) (7) as implemented by Armed Services Procurement Regulation (ASPR) 3-207 (1973 ed.). 10 U.S.C. 2304(a) (7) provides that negotiation may be used in lieu of formal advertising if the "purchase or contract is for medicine or medical supplies".

ASPR 3-207 (1973 ed.) provides, in part, that the authority of 10 U.S.C. 2304(a) (7) shall only be used when the supplies to be procured are particular to the field of medicine. Final payment on this contract was made on or about June 4, 1974.

Contract DSA120-74-C-2724

4. With respect to contract number DSA120-74-C-2724 I determined the following: this contract was awarded to Bristol by DSA on or about March 29, 1974, for a definite quantity of Ampicillin for oral suspension at a price of $152,775.79. This contract was negotiated by DSA pursuant to the authority of 10 U.S.C. 2304(a) (7) as implemental by ASPR 3-207 (1973 ed.). Final payment on this contract was made on or about July 26, 1974.

Contract DSA120-73-D-1769

5. With respect to contract number DSA120-73-D-1769 I determined the following: this contract was awarded to Bristol by DSA on or about January 23, 1973. This requirements type contract was executed to cover the needs of DSA for several different pharmaceutical products from January 23, 1973 through January 23, 1974 at an estimated price of $1,338,050.00. This contract was negotiated by DSA pursuant to the authority of 10 U.S.C. 2304(a) (7) as implemented by ASPR 3-207 (1973 ed.). Final payment on this contract was made on or about June 24, 1974.

6. Pursuant to the provisions of 10 U.S.C. 2313(b) the above-numbered contracts mentioned in paragraphs 3 and 4 incorporate by reference Standard Form 32, General Provisions, Supply Contract, November 1969, as modified by Defense Personnel Support Center Master Solicitation (Medical), DPSC Form 3539, January 1973, which, in turn incorporates by reference a clause entitled "Examination of Records by Comptroller General (1971 Mar.)" as set forth at ASPR 7-104.15 (1974 ed.), which provides as follows:

"EXAMINATION OF RECORDS BY COMPTROLLER GENERAL (1971 MAR)

(a) This clause is applicable if the amount of this contract exceeds $2,500 and was entered into by means of negotiation, including small business restricted advertising, but is not applicable if this contract was entered into by means of formal advertising.

(b) The Contractor agrees that the Comptroller General of the United States or any of his duly authorized representatives shall, until the expiration of three years after final payment under this contract or such lesser time specified in either Appendix M of the Armed Services Procurement Regulation or the Federal Procurement Regulations Part 1-20, as appropriate, have access to and the right to examine any directly pertinent books, documents, papers, and records of the Contractor involving transactions related to this contract.

(c) The Contractor further agrees to include in all his subcontracts hereunder a provision to the effect that the subcontractor agrees that the Comptroller General of the United States or any of his duly authorized representatives shall, until the expiration of three years after final payment under the subcontract or such lesser time specified in either Appendix M of the Armed Services Procurement Regulation or the Federal Procurement Regulations Part 1-20, as appropriate, have access to and the right to examine any directly pertinent books, documents, papers, and records of such subcontractor, involving transactions related to the subcontract. The term 'subcontract' as used in this clause excludes (i) purchase orders not exceeding $2,500 (ii) subcontracts or purchase orders for public utility services at rates established for uniform applicability to the general public.

(d) The periods of access and examination described in (b) and (c) above for records which relate to (i) appeals under the 'Disputes' clause of the contract, (ii) litigation or the settlement of claims arising out of the performance of this contract, or (iii) costs and expenses of this contract as to which exception has been taken by the Comptroller General or any of his duly authorized representatives, shall continue until such

appeals, litigation, claims or exceptions have been disposed of."

7. Pursuant to the provisions of 10 U.S.C. 2313(b) the above-numbered contract mentioned in paragraph 5 incorporates by reference Standard Form 32, General Provisions, Supply Contract, November 1969, as modified by Defense Personnel Support Center Master Solicitation, DPSC Form 3385, January 1972, which, in turn, incorporates by reference, a clause identified as "Examination of Records by Comptroller General (1971 Mar.)" as set forth at ASPR 7-104.15 (1974 ed.). This clause is identical to that cited in paragraph 6.

/s/ _____
JOHN G. BROSNAM

Washington D.C.

Subscribed and sworn to before me this 21 day of Aug, 1975.

/s/ Carl E. Berger
Notary Public

My Commission expires: July 14, 1976

UNITED STATES DISTRICT COURT
SOUTHERN DISTRICT OF NEW YORK

Civil Action No. 75 CIV 1334 (MEL)

BRISTOL LABORATORIES DIVISION OF BRISTOL-MYERS COMPANY, PLAINTIFF,

-against-

ELMER B. STAATS, COMPTROLLER GENERAL OF THE UNITED STATES, DEFENDANT,

and

UNITED STATES OF AMERICA, INTERVENOR-DEFENDANT.

AFFIDAVIT

CITY OF WASHINGTON)
) ss
DISTRICT OF COLUMBIA)

James D. Martin being duly sworn, deposes and says:

1. I am a certified public accountant and the Deputy Director of the Manpower and Welfare Division (MWD) of the General Accounting Office (GAO), and I have personal knowledge of the facts and proceedings herein.

2. The purpose of this affidavit is to show the rationale behind the request of the Comptroller General of the United States that he be permitted to examine Bristol's cost records which directly pertain to specific negotiated contracts which Bristol holds with the Government.

3. I am responsible for assisting the Director of MWD in the administration and operations of MWD for the Comptroller General of the United States. Under section 312 of the Budget and Accounting Act, 1921, 42 Stat. 25, the Comptroller General is responsible for investigating all

matters relating to the disbursement and application of public funds, for submitting to the Congress reports on the adequacy and effectiveness of the administrative examination of accounts and recommendations looking to greater economy or efficiency in public expenditures, and for reporting any expenditure or contract made in violation of the law. As a part of my duties I assist the Director of MWD in fulfilling his responsibility for the preparation of the reports and recommendations which concern the health-related programs of all departments and agencies of the Federal Government for submission to Congress under the cited statutory authority.

4. During 1972 and 1973, discussions were held by GAO representatives with representatives of the Pharmaceutical Manufacturers Association (PMA) and several of its member firms in connection with a proposed study of the drug industry contemplated by GAO as a part of its work in reviewing the Federal drug procurement system.

5. As a result of these discussions with PMA, GAO representatives made visits of 2 or 3 days to the facilities of 6 drug manufacturers, including that of Bristol Laboratories Division of Bristol-Myers Company (Bristol). These visits were designed to obtain for GAO an understanding of the drug manufacturing industry and to enable GAO to develop a meaningful approach for its contemplated study of drug procurement.

6. Although GAO's original plans for a comprehensive study of the salient economic and operational aspects of the drug industry were dropped because of a lack of cooperation from the industry, a more modest study is planned to be based on data obtained through the use of GAO access-to-records authority under specified negotiated contracts such as those cited in the Comptroller General's August 26, 1974 letter sent to Bristol (Appendix I). Similar letters were sent to 5 drug firms in addition to Bristol.

7. I know that during the visits to 6 drug firms, including Bristol, GAO representatives learned that in general the costs of the drug firm's normal pharmaceutical operations include a variety of costs such as manufacturing

costs, research and development costs, marketing and promotion costs, physical distribution costs, and general and administrative costs. In order to determine the bases of the prices of pharmaceuticals sold to the Government it is necessary to identify the nature and amount of all costs incurred by the contractor which are recovered by the contractor from the revenues derived by the sale of its pharmaceuticals.

8. It is my understanding that under the cost accounting systems utilized by the drug firms visited, the only significant costs which are assigned to individual products are manufacturing costs such as labor costs, material costs and, in some cases, certain manufacturing overhead costs. These costs, like the costs described in the paragraph next following, are recovered in revenues derived from the sale of pharmaceuticals. Bristol is willing to permit GAO to examine its records pertinent to such costs.

9. The drug firms we visited generally treat the costs they do not assign to particular products or contracts, as period expenses. These costs too are recovered through revenues generated from sales of their products including the sale of products to the Government pursuant to negotiated contracts such as those cited in the Comptroller General's August 26, 1974 letter. For example, PMA has stated at page 13 of its Annual Survey Report '71–72, Pharmaceutical Industry Operations Research and Development Activity (Appendix II) that the drug industry devotes a "significant portion" of its sales revenues (11.9 percent of the industry's 1971 sales) to research of new and improved ethical drug and biological products. These types of costs then are significant in amount and must be recovered in the sale of the company's products if the company is to make a profit on its investment.

10. The objective of GAO's study, as presently contemplated, is to review contract pricing by the Government's suppliers of drug items to determine the adequacy of the protection afforded the Government by the negotiation techniques used by the procuring agencies. The accomplishment of this objective is contigent upon GAO's

ability to gain access to the records needed to (1) ascertain the nature of the activities for which the drug firms are incurring costs, and (2) ascertain and verify the extent to which the costs of these activities affect the prices paid by the Government for items procured under specified negotiated contracts. Such costs include both those costs which the firms assign to particular products and those which, although they are incurred during the drug firm's normal operations and are recovered through revenues generated by sales of the firm's products, may not be assigned by those firms to particular products.

/s/ _____
JAMES D. MARTIN

Washington D.C.

Subscribed and sworn to before me this 21 day of Aug, 1975

/s/ Carl E. Berger
Notary Public

My Commission Expires: July 14, 1976

UNITED STATES DISTRICT COURT
SOUTHERN DISTRICT OF NEW YORK

75 Civ. 1334 (MEL)

BRISTOL LABORATORIES DIVISION OF BRISTOL-MYERS COMPANY, PLAINTIFF,

v.

ELMER B. STAATS, COMPTROLLER GENERAL OF THE UNITED STATES, DEFENDANT

AFFIDAVIT OF PAUL G. DEMBLING IN SUPPORT OF THE MOTION OF THE UNITED STATES FOR SUMMARY JUDGMENT

CITY OF WASHINGTON)
) ss
DISTRICT OF COLUMBIA)

Paul G. Dembling, being first duly sworn, deposes and says:

1. I am, and have been since November 17, 1969, General Counsel of the General Accounting Office. In that position I act as chief legal advisor to the Comptroller General of the United States, who is the head of the General Accounting Office. Under section 312 of the Budget and Accounting Act, 1921, 42 Stat. 25, the Comptroller General is responsible for investigating all matters relating to the disbursement and application of public funds, for submitting to the Congress reports on the adequacy and effectiveness of the administrative examination of accounts and recommendations looking to greater economy or efficiency in public expenditures, and for reporting any expenditure or contract made in violation of law. As part of my duties I am charged with reviewing generally, and particularly for

legal sufficiency, the reports and recommendations prepared for submission to Congress under the cited statutory authority.

2. There is included in negotiated contracts pursuant to 10 U.S.C. 2313(b) and 41 U.S.C. 254(c) a clause which provides in substance that the Comptroller General or any of his duly authorized representatives shall, until the expiration of three years after final payment, have access to and the right to examine any directly pertinent books, documents, papers and records of the contractor or his subcontractors involving transactions related to the contract or subcontracts (access-to-records clause). The access-to-records clause and the statute requiring its inclusion in negotiated contracts has been consistently used by the Comptroller General since enactment of the statute, and I know of no official congressional action to modify the statute or the access-to-records clause to limit their interpretation as asserted by the Comptroller General.

3. Examinations and audits of contractor records pursuant to the access-to-records clause have, as hereinafter detailed, resulted in (1) effecting a reduction in price in instances where such prices were regarded by representatives of the Comptroller General as excessive, (2) obtaining cost and price information which was given to procuring agencies for use in future negotiations and procurements, (3) providing a source for making recommendations to the Congress for Federal procurement legislation.

4. Examination by the General Accounting Office of contractors' records pertaining to negotiated contracts has resulted, in many instances, in the disclosure of profits considered by trained auditors in the employ of the General Accounting Office to be abnormally high. In a number of cases it has been possible, through the use of the contractual right to examine such records, to effect a reduction in such prices. For example, I have reviewed records of the General Accounting Office which show that the total value of contracts and subcontracts examined pursuant to the access-to-records clause by our Procurement and Systems Acquisition Division in fiscal years 1974 and 1975 to

date was $814,900,000. Of that amount, those records show that $4,964,437 was determined to be the result of overpricing. I have also reviewed records of the General Accounting Office which show that in fiscal years 1974 and 1975 to date, $5,004,135 was recovered from contractors and subcontractors as a result of earlier determinations of overpricing made pursuant to access-to-records clause investigations by the General Accounting Office. The General Accounting Office could not have performed the type of audits which led to the initiation of action to effect the recoveries, without the access to the contractors' records made possible by the inclusion in the contracts of the access-to-records clause.

In addition to leading to the described recoveries, the disclosure of profits deemed abnormally high has resulted in instances where the Comptroller General has advised the contracting agencies to negotiate prices more carefully or to obtain greater competition in future similar procurements.

Also, findings resulting from audits which included the examination of production cost records under contracts negotiated with the Government have provided a source for recommendations to the Congress for amending Federal Procurement legislation.

/s/ _____

PAUL G. DEMBLING

Subscribed and sworn to be before me this ___ day of ___ 1975.

My Commission expires:

_____

Notary public

UNITED STATES DISTRICT COURT
SOUTHERN DISTRICT OF NEW YORK

75 CIV 1334 (MEL)

BRISTOL LABORATORIES DIVISION OF BRISTOL-MYERS COMPANY, PLAINTIFF,

-Against-

ELMER B. STAATS, COMPTROLLER GENERAL OF THE UNITED STATES, DEFENDANT,

and

UNITED STATES OF AMERICA, INTERVENOR-DEFENDANT.

STATEMENT UNDER LOCAL RULE 9(g)

STATEMENT OF THE MATERIAL FACTS AS TO WHICH THERE ARE NO GENUINE ISSUES

The following is a statement of the material facts as to which defendants contend there is no genuine issue to be tried.

1. On or about January 23, 1973, plaintiff was awarded a contract with the Defense Personnel Support Center, Defense Supply Agency, for the sale of certain pharmaceutical products. Said contract is identified as DSA 120-73-D-1769.

2. On or about March 29, 1973, plaintiff was awarded a contract with the Veterans Administration, Marketing Division, Drugs & Chemicals, for the sale of certain pharmaceutical products. Said contract is identified as V797P-5929b.

3. On or about February 26, 1974, plaintiff was awarded a contract with the Defense Support Center, Defense

Supply Agency, for the sale of certain pharmaceutical products. Said contract is identified as DSA 120-74-C-2404.

4. On or about March 29, 1974, plaintiff was awarded a contract with the Defense Personnel Support Center, Defense Supply Agency, for the sale of certain pharmaceutical products. Said contract is identified as DSA 120-74-C-2724.

5. Each of the aforementioned contracts had incorporated therein a clause that provided, in part:

> "(b) The Contractor agrees that the Comptroller General of the United States or any of his duly authorized representatives shall, until the expiration of 3 years after final payment under this contract or such lesser time specified in either Appendix M of the Armed Services Procurement Regulation or the Federal Procurement Regulations Part 1-20, as appropriate, have access to and the right to examine any directly pertinent books, documents, papers, and records of the Contractor involving transactions related to this contract.
>
> "(c) The Contractor further agrees to include in all his subcontracts hereunder a provision to the effect that the subcontractor agrees that the Comptroller General of the United States or any of his duly authorized representatives shall, until the expiration of 3 years after final payment under the subcontract or such lesser time specified in either Appendix M of the Armed Services Procurement Regulations or the Federal Procurement Regulations Part 1-20, as appropriate, have access to and the right to examine any directly pertinent books, documents, papers, and records of such subcontractor, involving transactions related to the subcontract. The term "sub-contract" as used in this clause excludes (1) purchase orders not exceeding $2,500 (2) subcontracts or purchase orders for public utility services at rates established for uniform applicability to the general public."

6. The aforementioned contracts were not entered into by means of formal advertising.

7. In a letter dated August 26, 1974 from defendant Staats to Mr. Richard L. Gelb, President and Chief Executive Officer of plaintiff, defendant formally requested that plaintiff make available for examination by defendant all records of costs directly pertinent to the subject contracts.

8. On or about February 10 and 11, 1975 representatives of defendant Staats met with representatives of plaintiff in the latter's offices in Syracuse, New York. Although plaintiff made available for examination by defendant Staats' representatives those records it felt are directly pertinent to the subject contracts, said records were deemed incomplete by defendant Staats' representatives.

9. Under date of March 6, 1975, defendant Staats, in a letter to Mr. Richard L. Gelb, informed plaintiff inter alra that if it did not comply within 10 days with his formal request of August 26th, he would take "such action deemed appropriate." Weil Affidavit Exh. D.

10. The Comptroller General has a right of access to and examination of the following categories of records of plaintiff.

(1) Records relating to those costs assigned by plaintiff to the products purchased under the subject contracts, which industry representatives have indicated are limited essentially to manufacturing costs.

(2) Records relating to the methodology, and decisions involved in plaintiff's establishment of prices for the products purchased under the subject contracts.

(3) Records required to verify, to the extent deemed necessary, all data obtained during the course of any review conducted.

10. Plaintiff recovers costs for activities such as research and development, marketing and promotion, distribution and administration through revenues generated from sales of its products to the Government pursuant to negotiated contracts such as those cited in the Comptroller General's August 26, 1974 letter.

11. The only significant costs which are assigned to individual products are manufacturing costs such as labor costs, material costs, and in some cases, certain manufacturing overhead costs.

Dated: New York, New York
August 28, 1975

PAUL J. CURRAN
United States Attorney for the
Southern District of New York
Attorney for Defendants

By: /s/_____
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UNITED STATES DISTRICT COURT
SOUTHERN DISTRICT OF NEW YORK

Civil Action No.
75 CIV 1334 (MEL)

BRISTOL LABORATORIES DIVISION OF BRISTOL-MYERS COMPANY, PLAINTIFF,

-against-

ELMER B. STAATS, COMPTROLLER GENERAL OF THE UNITED STATES, DEFENDANT,

and

UNITED STATES OF AMERICA, INTERVENOR-DEFENDANT.

PLAINTIFF'S STATEMENT CONCERNING THOSE OF DEFENDANT'S "FACTS" AS TO WHICH THERE ARE GENUINE ISSUES*

The following statements** are made in opposition to defendant's statement under local rule 9(g).

7. The letter dated August 26, 1974 from defendant Staats to Mr. Richard L. Gelb, President and Chief Executive Officer of plaintiff, requested that plaintiff make available for examination by defendant records of costs that were not limited to ones that are directly pertinent to the subject contracts.

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*For its statement under local rule 9(g), plaintiff relies on the statement filed in support of its motion for summary judgment.

**Plaintiff's statements are numbered to correspond to defendant's statements of fact.

10.* This statement would be accurate if it read:

Plaintiff recovers expenses for activities such as research and development, marketing and promotion, distribution and administration through revenues generated from sales of its products without allocating them to any customer class, customer or contract.

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*This is in opposition to the second of defendant's statements numbered "10".

UNITED STATES DISTRICT COURT
SOUTHERN DISTRICT OF NEW YORK

Civil Action No.
75 CIV 1334 (MEL)

BRISTOL LABORATORIES DIVISION OF BRISTOL-MYERS COMPANY, PLAINTIFF,

-against-

ELMER B. STAATS, COMPTROLLER GENERAL OF THE UNITED STATES, DEFENDANT,

and

UNITED STATES OF AMERICA, INTERVENOR-DEFENDANT.

AFFIDAVIT

STATE OF NEW YORK)
) ss.:
COUNTY OF ONONDAGA)

LORNE C. D. MACBETH, being duly sworn, deposes and says:

1. I am Vice President-Marketing of Bristol Laboratories Division of Bristol-Myers Company and I have personal knowledge of the facts and proceedings herein.

2. I am a member of the Bristol Laboratories Pricing Committee which has as its responsibility the recommending of prices to be charged on government contracts.

3. The purpose of this affidavit is to set forth those costs considered by Bristol Laboratories in setting the prices on the products supplied under the contracts at issue in this litigation.

4. In setting prices to the government, Bristol Laboratories considers manufacturing costs such as: raw and

packaging materials, labor and fringe benefits, quality control and supervision; manufacturing overheads such as: plant administration, production planning, warehousing, utilities, and security; royalty expense; and, in a general way, the cost of delivery to the sites specified in the contract.

5. Bristol Laboratories does not consider expenses incurred for research and development; advertising and promotion; general and administrative; and distribution (except as set forth in Paragraph 4) in setting contract prices to the Federal Government.

/s/_____
LORNA C. D. MACBETH

Sworn to before me this 29th day of September, 1975.
/s/ Grace B. Maloney
Notary Public

UNITED STATES DISTRICT COURT
SOUTHERN DISTRICT OF NEW YORK

75 Civ 1334

BRISTOL LABORATORIES DIVISION OF BRISTOL-MYERS COMPANY, PLAINTIFF,

v.

ELMER B. STAATS, COMPTROLLER GENERAL OF THE UNITED STATES, DEFENDANT,

v.

UNITED STATES OF AMERICA,
DEFENDANT-INTERVENOR

April 6, 1976
10:30 a.m.

Deposition of BRISTOL LABORATORIES by RICHARD J. CORMIER, taken by Defendant pursuant to notice dated February 20, 1976 at the United States Attorney's Office, One St. Andrew's Plaza, New York, New York, before Elizabeth Whittet, a Shorthand Reporter and Notary Public of the State of New York.

[2] ATTORNEYS FOR PLAINTIFF:

ROBERT N. ENDRIES, Esq.
In-House Counsel, Bristol Laboratories
P.O. Box 657
Syracuse, New York.

WEIL, GUTTMAN & DAVIS, Esqs.,
Attorneys for Bristol Laboratories
60 East 42nd Street
New York, New York 10017

ROBERT L. SHERMAN, Esq.,

of Counsel

ALSO PRESENT:
JAMES D. MARTIN
DAVID P. BAINE
JOHN G. BROSNAN

ROBERT B. FISKE, JR.,
United States Attorney
Southern District of New York
NAOMI REICE BUCHWALD,
Assistant United States Attorney

* * * * *

IT IS HEREBY STIPULATED AND AGREED by and between counsel for the respective parties hereto that the sealing, filing and certification of the within deposition be waived; that such deposition may be signed and sworn to before any officer authorized to administer an oath; that all objections except as to form are reserved to the time of trial.

[2] RICHARD J. CORMIER,
having been first duly sworn, was examined and testified as follows:

EXAMINATION BY
MS. BUCHWALD:

Q Mr. Cormier, would you state your full name and home address for the record.

A Yes. Richard J. Cormier, 6358 Ledgewood Drive, Jamesville, New York 13078.

Q Mr. Cormier, by whom are you employed?

A By Bristol Laboratories.

Q In what capacity are you employed by Bristol Laboratories?

A As Vice President and Controller.

Q How long have you been employed by Bristol Laboratories?

A Approximately one year.

Q Have you held the position of Vice President and Controller the entire year?

A Yes, sir.

Q Mr. Cormier, before I begin let me just say, so that we understand each other, that when I refer to Bristol, unless I state otherwise, I am referring to Bristol Laboratories, and that when [3] I speak about production of drugs or ethical pharmaceuticals that I am speaking about the domestic production rather than the international production of drugs or ethical pharmaceuticals.

A Can you also clarify the time frame? Is there a certain period you are trying to cover?

Q My questions at this point do not have a particular time frame.

If I ask you a question and it turns out that something is true today but was not true at an earlier time, I would appreciate your specifying that if you note any difference.

Mr. Cormier, what is the corporate relationship between Bristol Laboratories and Bristol-Myers Company?

A Bristol Laboratories is a division of Bristol-Myers Company.

Q What are the product lines or business components of Bristol Laboratories?

A Are you referring to basic products? We are pharmaceutical manufacturers and suppliers.

Q Do you break down your production into any other more general components?

A Yes, our production is—our plant [4] production is produced by lot numbers for given products.

Q Focusing more on the types of products that Bristol Laboratories produces, do you divide Bristol Laboratories' production into any particular product lines, particular components?

A Our production is generally planned based on projected need. The production is really geared to a—by lots of specific products. In other words, today we may be producing a specific polycillin in a given size.

Q Focusing on the question more from an accounting perspective, do you divide the production of Bristol Laboratories into any particular lines of products?

A Not as such. If I am understanding you properly, we don't summarize and determine that a given product is produced in X quantities. We don't attempt to distinguish production by products per se.

MR. SHERMAN: It seems that we may be missing each other here.

Perhaps by way of examining him you could indicate what you are trying to ask.

[5] Q Mr. Cormier, in determining the profitability, the profits of Bristol Laboratories, do you utilize certain profit centers?

A Yes, we do.

Q What are those profit centers?

A Profit centers—I guess we might call them expense centers. We basically determine our profit on the total volume. We don't break it down by any other groupings, if that's what you are referring to.

Q Are you telling me that at no time or that no part of your accounting system breaks down profits into individual profit units?

A At the gross profit line we would break it down. We would have a record of estimated profits. The gross profit line reflects net sales less the cost of product.

Q What is the breakdown which you use at the gross profit line?

A There we would use individual product summaries.

Q Do you use any other breakdown than individual products?

A Yes. We might summarize by total [6] pharmaceutical products versus total veterinary products.

Q Mr. Cormier, what are ethical pharmaceuticals?

A I am not sure I can answer that question when you say "ethical pharmaceuticals." I assume that they are

probably a prescription type of pharmaceuticals.

Q In other words, is there a distinction between an ethical pharmaceutical and an over-the-counter drug?

A Yes, there is.

Q And the drugs which are involved in this lawsuit and the contracts involved here, those are ethical pharmaceuticals as distinct from over-the-counter drugs?

A Yes.

Q Does Bristol Laboratories produce over-the-counter drugs?

A Yes; very limited.

Q For accounting purposes, are your records divided as between over-the-counter drugs and ethical pharmaceuticals?

A Not really.

[7] Q Apart from ethical pharmaceuticals and over-the-counter drugs, does Bristol Laboratories produce any other products, types of products?

A Are you referring to products for humans?

Q It could be for humans.

A We have the veterinary products which are for animals.

Q Any other types of products? Do you have industrial products?

A No, we don't.

Q Mr. Cormier, are the drugs involved in the contracts at issue here produced entirely by the pharmaceutical component of Bristol Laboratories?

A I am sorry, could I hear that again?

Q Are the drugs involved in the contracts here at issue produced entirely by the pharmaceutical component at Bristol Laboratories, or more generally just by Bristol Laboratories?

A Those in question I believe were primarily produced by Bristol Laboratories at that time.

During the latter part of this contract there was a division made between Bristol Laboratories in some of the manufacturing sites. We [8] were set up as a separate division, so during late 1974 it is possible that some of these components could have been produced by a division at Bristol-Myers Company which was not a part of Bristol Laboratories.

Q What was that other division of Bristol-Myers Company?

A We refer to it as the Industrial Division.

Q Where is the Industrial Division located?

A Headquarters is located in Syracuse and there are plants in Puerto Rico, Syracuse, and I believe in Italy.

Q Apart from the Industrial Division of Bristol-Myers and Bristol Laboratories, does any other division or part of Bristol Myers produce ethical pharmaceuticals?

A I believe that some of the other divisions of Bristol-Myers produces ethical pharmaceuticals.

Q Do you know what those divisions are?

A I would assume that Meade-Johnson might have some prescription products. I am frankly not completely sure.

Q If we assume that the Industrial Division of Bristol-Myers participated in the manufacture of some of the drugs which are in issue in these contracts, does the Industrial Division of Bristol Myers therefore [9] accumulate the costs related to that manufacturing?

A Yes, it does. I probably should clarify that. It compares its costs to manufacture with the present estimated costs which we call a standard.

Q But in that process of comparison it records the costs actually incurred?

A No. We do not record actual costs by products.

Q Do you recall actual costs by division?

A By division, yes.

Q If the Industrial Division of Bristol-Myers partici-

pated in the manufacture of certain of the drugs which were sold by Bristol Laboratories to the Government, were the costs related to that production reflected on the books of Bristol Laboratories?

A The standard costs of that product in the Industrial Division was transferred to Bristol Laboratories. Any other costs would have been transferred as a separate division assessment.

Q What is a transfer as a division assessment?

A The Industrial Division produces product against predetermined standard costs. Any excess expenses or income that it might generate above or below these costs are transferred to Bristol Laboratories at the [10] indirect ratio to the per cent of volume that we utilize from that plant's production, from that division's production.

Q Does Bristol Laboratories do all the marketing of the ethical pharmaceuticals which were involved in these contracts?

A Yes, it does.

Q Does Bristol Laboratories do all the distribution of the ethical pharmaceuticals which were involved in these contracts?

A The distribution to—it does distribute to wholesalers who do further distribution of the product.

Q Perhaps let me ask it another way.

Does any other part of Bristol-Myers have any involvement in the distribution of the ethical pharmaceuticals which are involved in these contracts apart from Bristol Laboratories?

A Not within the United States.

Q Mr. Cormier, does Bristol Laboratories do all the company's research and development for ethical pharmaceuticals which are produced by Bristol Laboratories?

MR. SHERMAN: Excuse me, when you refer [11] to the companies do you mean Bristol-Myers Company or the Division?

MS. BUCHWALD: I may have misspoke. Let me try

the question again.

Q Mr. Cormier, does Bristol Laboratories do all the research and development for those ethical pharmaceuticals which are produced by Bristol Laboratories.

A I am sorry. I know you said it right, but could you repeat that?

(Question read.)

A Not necessarily.

Q What other division or part of Bristol-Myers may do research and development for ethical pharmaceuticals which are produced by Bristol Laboratories.

A Meade-Johnson Company can conceivably do some work in this area, BMCID, Division of Bristol-Myers which is the International Division.

MR. ENDRIES: That is an acronym for Bristol-Myers Company International Division.

Q Mr. Cormier, does Bristol Laboratories have a Pricing Committee?

A Yes, it does.

Q Are you a member of that Committee?

A Yes, I am.

[12] Q Who else are members of the Bristol Laboratories Pricing Committee? Can you tell me their names and their titles?

MR. SHERMAN: Excuse me. I think on this question we should define the time period involved. Do you want the current Committee?

Q Let's take the current Committee.

A You want the names and titles?

Q Right.

A Lauren MacBeth, Vice-president of Marketing, John Shaw, General Product Manager, Tom Connelly, I believe it is National Sales Manager and the Group Product Manager for the individual products in question would sit in on the Committee. There are two such Product Managers, Gary Gibson, he was Group Product Manager of, I would

say, primarily Antibiotics. Neither he or Allen Fox, who is Group Product Manager—I don't have the exact breakdown of what products each of these gentlemen have.

In addition to that, Richard Jackson, Director of Financial Planning, Raymond Egan, General Manager of the Veterinary Division, Robert Wenzel, Vice-President of Materials Handling, Otto Nonnenmann, Director of Manufacturing.

[13] I should say Robert Endries is a non-voting member of the Committee. He is Chief Counsel for Bristol Laboratories.

Q Mr. Cormier, are all of these gentlemen whom you have just named as members of the Pricing Committee are their positions with Bristol Laboratories?

A Yes, they are.

Q Apart from the fact that perhaps some of the gentlemen holding these various positions has changed over the years, did the persons holding the same positions sit on the Pricing Committee back in 1973 and 1974, if you know?

A This Pricing Committee was formed, I believe, in the latter part of 1974.

Q Prior to the latter part of 1974 when this Pricing Committee was formed, was there some other body at Bristol Laboratories that performed essentially the same function the present Committee performs today?

A Basically the Product Manager and his market superiors probably accomplish the same thing.

Q What is the function of the Pricing Committee and its informal predecessor?

A To pass on the acceptability of prices being proposed for new products or existing products, [14] particularly in the area of bids.

Q From whom does the Pricing Committee obtain the information upon which it basis these pricing decisions?

A Generally from the Pricing Manager. In some situations it receives it from the Manager of Government sales,

I believe.

Q Are either of those gentlemen, the Pricing Manager or the Manager of Government Sales, members of the Pricing Committee?

A No, they are not. I might add that information on new products would probably come from the Product Managers.

Q What is the function of the job of a Pricing Manager?

A He basically files the formal bids and the informal bids of our customers. He loads the bid prices into the computer. He records as much as possible, the results of prior bids.

Q What is the function or the job of the Manager of Government Sales?

A He is responsible for following government requirements and making sure that we bid on all government requirements. He coordinates the activities [15] of those sales people in the field who might call on government facilities.

Q Incidentally, Mr. Cormier, do you know the approximate amount of sales which Bristol Laboratories makes to government contracts as distinct from non-government contracts?

A No, I don't.

Q Are there any records at Bristol Laboratories that would give the answer to that question?

A Not without a great deal of research.

Q Are there any other committees at Bristol Laboratories that are concerned with pricing decisions?

A No.

Q Who makes the final decision as to pricing?

A In most cases it would be the Pricing Committee.

Q In cases when it is not the Pricing Committee, who is it?

A It is conceivable it could go before the Operating Committee.

Q Is that an Operating Committee of Bristol Laboratories?

A Of Bristol Laboratories.

Q Who sits on the Operating Committee? Not [16] their names, give me their positions.

A Generally the people who report to the President of the company.

Q Just briefly what positions do these people have?

A The Vice-president of Materials Handling, Vice-president of the Controller, Vice-president of Marketing, Director of Manufacturing, Chief Counsel, Director of Quality Control, Director of Research, Vice-president in charge of Research, Vice-president of Personnel.

Q Apart from yourself, which officers of Bristol Laboratories are concerned with financial matters?

A The President, of course, is involved in all phases of the business including financial activities.

Q Is it just you and he primarily?

A In terms of financial responsibilities, yes.

Q What is the involvement, if any, of Bristol-Myers Company in determining the pricing of products produced by Bristol Laboratories?

A Today they are basically not involved, however until probably five or six months ago they did [17] review any price increases that were proposed, and I believe, were notified and passed on prices of new products.

Q Who at Bristol-Myers in this period up to six months ago would have been involved in passing upon price increases or new product prices?

MR. SHERMAN: Before the witness answers that question—I have really been sitting back rather quietly. I would like to just state that the deposition that was noticed, and according to Judge Lasker's decision, is a fairly narrow one. I have not been objecting, and I don't intend to start objecting to the scope of the examination, but I wonder if we could somehow home in on the real issues involved and the methods and procedures of ac-

counting and allocation.

We seem to be drifting further and further afield.

MS. BUCHWALD: I don't think that we are drifting afield, Mr. Sherman. I think we are directly within the scope of Judge Lasker's decision since the deposition notice specifically refers to methods and procedures for allocation and recovery of costs.

Surely, I think we would all agree that it is from the prices which are charged for goods, [18] drugs produced by Bristol Laboratories, that is, costs to recover. I don't think that we will be too far along this particular line. We don't have too much to go on this particular line.

Anyway, there was a question pending, I think.

(Question read.)

A Mr. C.F. Michaelis, Mr. L. Brokaw, and I am not sure who else was on that Committee.

Q Mr. Cormier, when the Pricing Committee is considering the price to be charged for a new product, let's say, what type of information does it have before it?

A It would have estimated cost of a product. It would have probably competitive products and pricing. It would possibly look at other related products within the division, costs and some prices, standard manufacturing costs that is.

Q When you said before estimated costs, could you describe that more fully?

A The Engineering Departments and the Cost Accounting Departments would collaborate to estimate the material, the labor and the overhead costs of a planned new product introduction, cost to manufacture that [19] product.

Q Do you have before you any data on the cost that had previously been incurred to create the product?

MR. SHERMAN: When you use the word "you", do you mean the Pricing Committee?

MS. BUCHWALD: Yes.

A I just want to be sure I understand the question.

Q Do you mean costs which we incurred prior to introducing the product?

Q Right.

A One clarification I think I should make is I mentioned that we estimated the cost, and I mentioned overhead. This is strictly manufacturing overhead.

Q Mr. Cormier, does Bristol Laboratories accounting system identify the results of operations attributable to its domestic ethical pharmaceutical business?

A Yes, it does.

Q Does the accounting system of Bristol Laboratories identify any costs by business segment? In this case, I am referring to, as we discussed earlier, the Pharmaceutical Division. We have the [20] Veterinary Division. Are any of your costs identified to those various business segments of Bristol Laboratories

A We make an attempt on a limited basis to identify some of the costs related to pharmaceutical versus veterinary business.

Q Is that the only division that you attempt to make?

A That all depends where on the profit and loss statements you are referring to. We have no—in fact, at our present taxed profit line we have no distinction between any of them.

Q But that is not exactly my question. What I am asking is whether your accounting system at some stage, not necessarily your tax stage, identifies any costs by these product divisions?

A I should point out that all of our product costs, which reflect our manufacturing costs, are handled on a standard cost basis. We do not attempt to determine the actual costs by groupings. We do know that costs are based on standards, but any deviations from those standards I am not basically identifying by product groups.

Q Let me ask you this then:

How do you arrive at your standard costs?

[21] A Standard costs—we estimate.

Say in August or September of one year we estimate what our raw material, packaging materials, labor machinery costs and factory overhead costs would be, and this estimate forms the standard cost which then is what is measured against the income to determine gross profit margins.

In addition to this, grouped together we have any variations that occur when those estimated costs are put into what we call a variance account. That variance account does not attempt to determine what products those variances apply to.

Q In determining the standard costs and your making an estimate, is that purely an estimate looking to the future, or is there some function in that estimation based on past experience?

A The estimate is based on what we expect that product to cost it in the year that it would be produced, the average cost during that year. Past history in some cases would be a factor in determining some of the components of that estimated cost.

Q Does the accounting system of Bristol Laboratories identify any costs by product?

A There again, it identifies the standards, [22] but in the manufacturing costs it does not further break down the variances from that standard by product.

Q Does the accounting system of Bristol Laboratories identify any costs by contract?

A None at all, to my knowledge.

Q Does the accounting system of Bristol Laboratories identify any cost by class of customer?

A It could down to the gross margin line which merely is a reflection of net income less the manufacturing cost of the product at standard plus royalty expense.

Q Does the accounting system of Bristol Laboratories identify any costs by government versus non-government contracts?

A The only place it ever attempts to get a comparison

here again is by reflecting net sales versus standard costs plus royalties which would bring you down to the gross margin line.

Here again, it cannot, it does not, attempt to determine the exact cost of that product.

Q Mr. Cormier, in your counsel's 9-G statement, which is one of the papers which has been filed in this lawsuit, it was stated that certain expenses such as research and development were recovered from sales, [23] "without allocating them to any class, customer or contract."

What do you understand the meaning of the word "allocate" to be as used in that quotation?

A I assume what he is saying there is no attempt to determine what part of research expenses might apply to any given product or any given contract or any customer group.

Q Is the word allocate a word that can be used interchangeably with the word assign?

A I would think in most cases.

Q Mr. Cormier, just so that we talk the same language, what does the term period expense mean?

A Many companies operate what is called a direct cost system. In a direct cost system the method of accounting attempts to determine the estimated cost of a product based on variable manufacturing costs only. Such things as materials, which normally might vary, where the cost might vary directly with the volume, some direct labor where the cost might vary directly with the volume, the period costs are generally the costs which are considered somewhat fixed and can't be exactly allocated to a given product.

[24] In that cost system period costs are identified as primarily manufacturing overhead costs which do not bear an equal relationship to the individual products or the volume situation in any given product.

Q What was the term that you used to describe this item of accounting?

A Direct cost system.

Q Does Bristol Laboratories operate under a direct cost system of accounting?

A I believe it did at one time, but today we do not. We operate under full absorption manufacturing cost system.

Q Mr. Cormier, what does the term direct product margin mean?

A Are you taking that from any given report you are looking at? I would like to put it in context.

Q I am taking it from some of Bristol Laboratories accounting forms—that is the best way I can describe them—which were, as I understand it, furnished by Bristol Laboratories to representatives in the General Accounting Office.

There is a line on one of these, I think, which appears in more than one place which says, "Direct product margin," and I would just like to know [25] what you mean by that. On the sheet I am going to give you there are some handwritten words. Those are not from his Bristol Laboratories, those are ours.

MR. SHERMAN: I think perhaps we should have that marked as an exhibit.

MS. BUCHWALD: Sure. No problem at all.

Why don't we mark as an exhibit of the United States seven sheets which apparently are some forms used by Bristol Laboratories in connection with their accounting system.

(Seven sheets being forms marked Government's Exhibit 1 for identification.)

Q Let me ask you this, Mr. Cormier, are you familiar with Government's Exhibit 1?

A Yes, I am.

Do you want me to go through all parts of it?

Q No, basically does this look familiar to you?

A Yes. The direct product margin as reflected on page I-2 of this document refers to gross profit margin, gross margin.

Q Does Bristol Laboratories accumulate direct manufacturing costs?

A I would like to distinguish that. When [26] you speak of direct manufacturing costs—we just talked of a direct costing system. I assume you are not referring to direct costs versus fully absorbed costs.

Q I am really going to get a line of questioning in which I am going to ask you of various types of costs, and ask you whether you accumulate those kinds of costs?

A Bristol Laboratories operates on a standard cost system which estimates the costs of each product at a point in time before a year begins, and generally that cost is used during the whole year in question as the cost in attempting to determine any gross profit to the company.

The cost variations that occur from this standard cost are categorized as variances. Those variances are accumulated in a group, for the most part, as part of other manufacturing costs. The only other costs reflected in the cost of goods sold is the royalty cost which can be calculated by product.

Q Just so that there is no confusion, are direct manufacturing costs among those standard costs which Bristol Laboratories calculate?

A I guess I would have to assume when you [27] say direct costs that you are referring to that portion of the standard costs which we can identify as direct costs versus absorbed costs.

Q Yes. I believe that is one of the distinctions I am trying—

A With that in mind, I guess I need the question restated.

Q The question is, considering the direct manufacturing costs as something distinct from what you call absorbed costs, are direct manufacturing costs among the standard costs which Bristol Laboratories accumulates?

A The direct costs are accumulated primarily as a variance to the standard cost.

Q And among those are direct manufacturing costs as one of the variances to standard costs?

A Yes.

Q Are manufacturing overhead costs accumulated as a variance to standard costs?

A Yes, they are.

Q Are general administrative costs accumulated as a variance to standard costs?

A Generally administrative costs do not fall in the manufacturing costs category.

[28] MR. SHERMAN: Excuse me. So the answer to that is no?

THE WITNESS: The answer is no.

Q Are general administrative costs accumulated by Bristol Laboratories?

A In total, yes.

Q Research costs accumulated by Bristol Laboratories?

A Yes, in total.

Q How about development costs, are those accumulated by Bristol Laboratories?

A They could be part of research costs.

Q Are research costs and development costs accumulated separately by Bristol Laboratories?

A Not really.

Q I ask that because on page 1 of Government's Exhibit 1 there are two separate headings, it appears to me, for research costs and development costs under a more general heading, "Not Charged to Profit Centers."

A This form, I-1, is apparently an old form, and at present I am not sure what kind of costs they were reflecting under this development cost.

Q Are advertising and promotion costs accumulated by Bristol Laboratories?

[29] A Yes, they are.

Q Perhaps to shorten things, could you tell me which costs specifically are included in the standard costs?

A None of these that you have just mentioned are included in the standard costs.

Q You are talking about—not included are advertising and promotion, general administrative, research and development?

A That's right.

Q What about manufacturing overhead?

A Manufacturing overhead is included in standard costs and variances.

Q And what we called before direct manufacturing costs, that's also included in standard costs?

A And in variances.

Q Are any other costs included in your standard costs?

A Royalty costs.

Q Any others?

A No.

(Discussion off the record)

A I am sorry, I should correct that. The royalties are not part of the standard costs. They are reflected [30] within the cost of the goods sold portion of the P&L statement, but they really are a separate calculation and not part of the standard costs.

Q Are direct manufacturing costs allocated to products?

Let me rephrase that.

Are all costs which are included in what you call standard costs, are those costs allocated to products?

A Are you referring to actual costs, or are you referring to estimated costs?

Q Let's do one at a time. First the standard costs, are those costs allocated to particular products?

A In the standard costs which are estimated costs, they are allocated to the standards.

Q And the variances, are those allocated to products, the variances from the standard costs?

A No.

Q To what, if anything, are variances from the standard costs allocated?

A They aren't. Variances become a central variance account.

Q Of Bristol Laboratories?

[31] A Right. We could have some type of variances, but not in any way allocated by product.

Q Are research and development costs allocated to any product line or product of Bristol Laboratories, or are research and development costs solely allocated to Bristol Laboratories as a totality?

A They are not allocated.

Q Is the same true for general administrative costs? Are those also unallocated?

A Unallocated.

Q The same for advertising and promotion costs or not?

A In one of our internal reports used for compensation purposes, we do attempt to identify some of the advertising promotion costs by product, not by customer type, but by product.

Q How do you accumulate costs which are not allocated?

A We accumulate them by natural expense classification and total them up to reflect them on the profit and loss statement.

Q What is natural expense classification?

A We might acculumate cost by labor, fringe benefits, travel expense, and total them up for a given [32] category.

Q You spoke earlier about your variances from standard costs. How often do you accumulate the variances to standard costs?

A Variances are accumulated as each transaction is recorded. For example, if we purchased a given raw material and the invoice price is different from that which is used in the standard costs, that variance is recorded at the time the invoice is processed.

Q So there are particular records which reflect these variances from the standard costs?

A Yes. I believe that this is computed by the computer.

Q I may have asked you this earlier, I just don't recall.

Are any costs of Bristol Laboratories allocated exclusively to non-government contracts?

A No.

Q Does the company allocate or assign costs to products or to product lines for any internal management purpose which costs may not be assigned as part of the company's regular cost accounting system, apart from the advertising and promotion costs which you mentioned a few minutes ago?

[33] A That's kind of broad.

(Question read)

A Only as shown on page I-2, Exhibit 1.

Q Since I didn't read Exhibit I-2, why don't you describe to me in words what internal system you have of allocation with respect to my last question.

A The manufacturing costs and royalties without variances, we attempt, for internal purposes, to measure those against a given product, not against any customer groupings, but against a given product. The distribution, advertising and promotion costs we attempt to assign to certain products. Some portions can be identified directly with products although not with customer groupings.

Other portions must be allocated. Some of the sales costs and marketing costs we attempt to allocate for internal measurement of some of our people on an estimated basis to products, not to customer groupings, but to products.

Those are basically the major costs that we attempt in any way to allocate or identify by product.

Q Do you make any internal efforts to allocate research and development costs to products?

A Can I have that again?

[34] Q Do you make any attempt to internally allocate research and development costs to products?

A No, we do not.

Q To product lines?

A No, we do not.

Q Do you have any internal system for allocating research and development costs in any way?

MR. ENDRIES: Within Bristol Laboratories.

A To products?

Q Any way, any internal system, allocate research and development costs within Bristol Laboratories.

A We in the past year and a half, I believe, we have attempted to estimate costs of research based on projects. We have no historical costs before that. These are not products for the most part, these are compounds for the most part that we hoped would eventually become products.

Q Do you treat research and development costs as period expenses?

A Yes.

Q Are all research and development costs allocated to Bristol Laboratories, incurred by Bristol Laboratories, allocated by Bristol Laboratories?

A No.

[35] Q Or some research and development costs incurred by Bristol Laboratories, allocated to Bristol-Myers?

A To other divisions of Bristol-Myers.

Q What other divisions?

A Meade-Johnson Company, BMCID, which is the International Division, and possibly Westwood.

Q How do you determine when you are going to allocate these research and development costs to other divisions of Bristol-Myers?

MR. SHERMAN: I would just like to state when we use the word "divisions," the witness is not a legal expert. There may be subsidiary corporations and not real divisions.

MS. BUCHWALD: All right.

(Question read)

A There are two ways which we might do this. One, if another division requested services from our research and development group, we would charge them for the service. Also, there are certain research expenditures which are classed as future product investment. Those research costs are allocated to the division within the PHI group.

MR. ENDRIES: Pharmaceutical, Health Care and [36] International, PHI.

Q Has this allocation of some research and development costs to other divisions of Bristol-Myers been the practice over the last ten years, or is this a very recent practice?

A I believe there have been some changes in the practice over the last few years. I am not sure what the practice was prior to the last few years.

Q Over the last few years it has been the practice to do some allocation of research and development costs to other divisions of Bristol-Myers?

A Yes.

Q Why do you treat research and development costs as periodic expenses rather than as an indirect manufacturing overhead?

A Research expenses do not really apply to products that were currently selling. They apply to products we hope some day will come into the marketplace. Therefore, there is no real way to apply them against any products we are selling at present.

Q I assume at certain times at least there is continuing

research or development with respect to a current product. In that case, do you assign a computering research cost to the product or nonetheless [37] continue to treat it as a period expense?

A We still treat it as a period expense because the additional research is undoubtedly for a new claim that doesn't exist, and therefore it doesn't apply to the existing product.

Q Is there any limit on the amount of money budgeted for research and development for Bristol Laboratories?

A Yes, there is.

Q How is that limit established?

A Through a budgeting procedure and controls which are subsequently imposed on the spending of funds.

Q Generally speaking, what is the basis of the restriction on the amount of money that can be spent for research and development?

A The basis is probably what we could afford.

Q Net sales of ethical pharmaceuticals identified with the pharmaceutical component of Bristol Laboratories?

A I am not sure I understand the question.

Q What I am trying to find out is, is there a breakdown of net sales by component within Bristol Laboratories, veterinary sales, pharmaceutical sales?

A We do have sales information on the product [38] groupings.

Q Does the Bristol accounting system identify sales by product?

A Yes, it does.

Q Does the Bristol accounting system identify sales to particular types of customers?

A Yes, it does.

Q How does Bristol Laboratories make its customers aware of its prices, prices of its ethical pharmaceuticals?

A They distribute price lists.

Q Are there different price lists for different types of

customers?

A Yes. There is a price list for wholesale accounts. There is a price list for direct accounts. I am sure that there are some price lists issued to some of the government agencies.

Q What specific factors are considered in establishing the price for a product?

A Which price?

Q You can tell me whether it matters whether it is going to be a product sold to a wholesaler, a direct account or a government agency. I was trying to do it step by step. Generally what factors do you [39] consider in setting a price, and on top of that, how do you vary your price by the type of customer to whom you would be selling the product?

A I believe previously I indicated the factors we considered in selling prices were the estimated standard costs. Competitive pricing, our own pricing of similar products. I believe that's part one of the question.

The price to the wholesaler was generally 5 percent lower than the price to the direct accounts. Where there is not a bidding situation, the price to the government we had listed would normally be the wholesale price.

Q What factors go into this 5 percent take-off of percentage discount from direct accounts to wholesale prices?

A Are you asking why we have a 5 percent lower price than wholesalers?

Q Right.

A They are attempting to sell to the drug stores. We do sell to some of the drug stores directly. In order to give them some incentive, we given them a lower price to permit them to cover their costs, to sell to these same customers and hopefully make a profit.

[40] Q You mentioned before that the factors that you considered in setting a price were the estimated standard costs, competitive pricing, and your own price for similar products. Is there any standard way in which these factors weighed one against the other?

A There is no formula whatsoever used in setting prices.

Q With relationship to costs, is there any floor for the price level of a particular product?

A No.

Q Do you, in setting your prices, work under a gross margin figure or direct product margin figure?

A We consider what a gross margin might be, the difference of the prices, if that's what you are asking.

Q I realize that in every case you probably calculate that, but is there any minimal gross margin figure which you must recover before you will sell a product?

A No.

Q Is there any documentation for the pricing decisions with respect to particular products? For example, are there minutes of the Pricing Committee?

A There is a report submitted for the entry of a price into our computer which indicates the prices [41] that were approved in a pricing meeting.

Q But what you feed into the computer is the end result, isn't it? It is the price for the drug that's going to be charged?

A Yes.

Q That's not exactly what I am asking you. What I want to know is, is there any documentation or record of the decision-making process by which you arrive at the price to be charged for a particular drug?

A Do you mean the logistics we used, or are you talking about the end result of our decision?

Q I am not interested in the end result of your decision, which is, I assume, published in your price lists. I am talking about the decision-making process. How did you arrive at that judgment as to what price to charge? Are there documents or other records which would reflect the factors that you considered in arriving at a price, maybe how you weighed one against the other or the like?

A There are no official records, but we could conceivably be given a sheet of paper which would indicate the competitive price lists, our own standard costs, a proposed price, and that we would get conceivably at a meeting. We would use that in making [42] a judgment as to where that price should be. I don't know where—most of mine are tossed out after we make the decision. I don't know if anybody keeps them.

Q Is there a secretary to the Pricing Committee?

A Yes, there is.

Q Does the secretary keep any minutes of the Pricing Committee meetings?

A She makes a record for the participants of the results of the meeting.

Q Does that record ever contain any of the factors that were considered in reaching the result of the meeting?

A It could conceivably.

Q Are there certain occasions on which you decided not to market a certain product after having a meeting with the Pricing Committee?

A When you used the word "market," that implies it is a new product, and we are trying to decide whether we should put it on the market or not put it on the market, or are you referring to a situation where we have a specific quote to make and we decide not to quote?

Q I am not thinking about the bid situation. I am thinking more of either a determination to put a new [43] product on the market, or perhaps another determination to change the price of the product. After the discussion of the Pricing Committee in which you have discussed what price you will have to charge, presumably taking into account your costs, you then decide not to sell this product.

A I don't recall any such situation. It is conceivable that could happen, but unlikely, I would say.

Q Are special considerations which have been given by Bristol Laboratories to meeting certain government requirements for pharmaceuticals taken into account when

Bristol Laboratories establishes its prices to the government?

A If there is a significant change in process or materials, we very likely would consider that factor.

Q Is it the aim of Bristol Laboratories to operate profitably?

A I would say yes.

Q With reference to any and all of the records which you maintain, can you determine the profitability of the product grouping of pharmaceutical products of Bristol Laboratories?

A Not on a pre-tax basis.

Q Can you do it on a post-tax basis?

[44] A No, less so.

Q Again using all of the records you maintained, can you determine the profitability of any particular drug produced by Bristol Laboratories?

A No.

Q Is profitability a factor in deciding whether to market a new drug?

A I don't know that that question ever gets raised in that context. We assume that when we bring a product to market it will help us to offset some of our expenses which we incur.

Q On what basis do you determine to adjust the price of an existing product?

A Is this generally or does this relate to bidding situations?

Q First let's take generally.

MR. SHERMAN: Prices to the government?

MS. BUCHWALD: I am really asking somewhat more generally about your determinations of adjusting the prices for a particular product which, as I understand Mr. Cormier's answers, the government will get a certain percentage discount off of the price list for direct accounts.

What I am trying to ask him is:

[45] Q Generally, in arriving at the price which is going to be included on that price list, and presuming now a situation in which there has been a decision to change the price on the price list, which I presume there is from time to time, what factors go into the adjustment of that price?

A Competitive pricing and cost increases. They are probably the major factors considered.

Q Is there any consideration given to the profitability of the product—

A We don't know what the profit is on the product.

Q You stated before that it was your hope that from sales of products, new products, you would offset expenses. I assume that to operate profitably you must recover costs and expenses from sales revenues, is that correct?

A Yes.

Q Are sales revenues affected by the prices that you charge for products?

A Yes, I would say so.

Q How do you make sure that the prices charged are sufficient to recover your costs and expenses and still have to make a profit?

[46] A We can't determine this by individual products. We historically know what our total sales are, what our total expenses are. That's why many of our comparisons are made on some of our historical information insofar as what kind of prices have succeeded in giving us a total overall profit in the division.

Q Mr. Cormier, what methodology is employed by Bristol Laboratories in establishing prices to be charged to the government under negotiated contracts?

A Can you give me that once again? In negotiated contracts?

Q Right. What methodology is employed by Bristol Laboratories in establishing prices to be charged to the government under negotiated contracts?

MR. ENDRIES: Are you using the term of art "negotiated" as opposed to advertised contracts?

MS. BUCHWALD: We are talking in terms of the contracts that we have in this lawsuit.

A These are bid contracts, are they not, which are not negotiated. They are bid contracts.

MR. BROSNAN: They are negotiated.

MR. ENDRIES: That's the way I look at them. We look at them—

THE WITNESS: I would understand them to be [47] bid contracts.

MR. ENDRIES: Our methodology is the same whether we are talking about responding to an advertised contract by the government or a negotiated contract by the government.

Q Just describe what that response is in methodology.

A We would look at the estimated standard cost for the product in question. We would look at historical bidding on our part and on the part of our competition, and basically these are the factors that would allow us to render a decision on what price should be bid for a given contract.

Q Are revenues from Bristol Laboratories' sales of pharmaceuticals to the government comingled with revenues from Bristol Laboratories' sales to other customers?

A Yes, they are.

Q Can Bristol Laboratories identify through its accounting system which revenues are generated from sales to the government and which revenues are generated from sales to other customers?

A Yes. It can determine the revenues from sales to government versus revenues from sales to other [48] customers.

Q Do government sales revenues cover, along with other sales revenues, all business expenses incurred during a financial reporting period?

A I think you will have to restate that.

Q Do government sales revenues cover, along with other sales revenues, all business expenses incurred during a financial reporting period?

MR. ENDRIES: Normally, yes, if they are profitable.

A If they are profitable.

Q If they are profitable." Is the clarification with the word "normally"?

A Yes.

Q Mr. Cormier, is it accurate that revenues generated from government sales contribute, along with revenues from sales to other Bristol customers, to the recovery of all costs of doing business during that period, as we have just discussed, notwithstanding the fact that these costs may or may not be identified and assigned to any particular business segment or product line or particular product?

Would you like the reporter to read that back?

[49] (Question read)

A I don't believe that we have any way of really telling, except for the fact that we received X amount of dollars in income and expenses recorded during this period, an amount for X number of dollars, and the difference either reflects a profit or a loss. I don't understand that. We can't really determine what income applies to what expenses.

Q I think you just told me a moment ago when I asked you the question, do government sales revenues cover, along with other sales revenues, all business expenses incurred during a financial period. You answered, "Normally, yes," presuming that you operated profitably. I just asked you really the same question and added the observation that some of those costs may not be identified to particular lines of business or specific products.

MR. SHERMAN: I think the second question asked if revenues generated from government contracts went toward recovering all expenses. Mr. Cormier said he has no idea which expenses government revenues went toward recovering. That was slightly different from the first ques-

tion. The answer to the first question is still yes, all other revenues cover all expenses. [50] He can't tell you, I believe, correct me if I am wrong, in the second question, whether government revenues go toward all expenses, which is, I think, the way the second question read.

MS. BUCHWALD: I think the second question noted and asked whether—

MR. SHERMAN: We can have it reread.

(Question read)

A It does include both, I am sorry.

Q So the answer then to the —

A The answer would be, normally when our total revenues exceed our total expenses for a given period.

(Short recess)

MS. BUCHWALD: Mr. Cormier, I would just like to say that we don't have any further questions for you at this time.

MR. SHERMAN: I would just like a further two-minute break, and I would just have about five minutes' worth of questions.

(Short recess)

EXAMINATION BY MR. SHERMAN:

Q Mr. Cormier, you said you first started working for Bristol Laboratories in 1974?

A March of 1975.

[51] Q 1975, I am sorry.

Are you thorougly familiar with Bristol's accounting methods and procedures currently?

A Yes, I am.

Q Are you also familiar with the methods and procedures that were used prior to the date that you were employed by Bristol?

A Yes, I am.

Q Could you just briefly tell us how you became familiar and knowledgeable to those procedures?

A I spent a good deal of time reviewing documents, reviewing procedures with the people in my organization. In essence, the accounting system at Bristol Laboratories is not very different from the accounting systems found in many manufacturing operations which I have worked with over the past twenty-five years.

Q I believe you stated earlier that in arriving at gross profit margin, that Bristol considers standard costs and royalties by product. Does it do that by type of customer?

A In a few instances we have attempted to arrive at a gross profit margin by customer group. Normally gross profit is reviewed by product.

[52] MR. SHERMAN: That's all.

MS. BUCHWALD: I have no further questions.

(Time noted: 12:50 p.m.)

Subscribed and sworn to before me this___day of___ 1976.

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[53] CERTIFICATE

STATE OF NEW YORK)
) ss
COUNTY OF NEW YORK)

I, ELIZABETH WHITTET, a Shorthand Reporter and Notary Public within and for the State of New York, do hereby certify:

That, RICHARD J. CORMIER, the witness whose deposition is hereinbefore set forth, was duly sworn by me and that such deposition is a true record of the testimony given by such witness.

I further certify that I am not related to any of the parties to this action by blood or marriage, and that I am in no way interested in the outcome of this matter.

IN WITNESS WHEREOF, I have hereunto set my hand this 8th day of April 1976.

/s/ Elizabeth Whittel

[54] **WITNESS INDEX**

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Richard J. Cormier	2

EXHIBIT INDEX

Government		*Page*
1 (id)	Seven sheets being forms.	25

UNITED STATES DISTRICT COURT
SOUTHERN DISTRICT OF NEW YORK

75 Civ. 1334 (MEL)

BRISTOL LABORATORIES DIVISION OF BRISTOL-MYERS COMPANY, PLAINTIFF,

-against-

ELMER B. STAATS, COMPTROLLER GENERAL OF THE UNITED STATES, DEFENDANT.

and

UNITED STATES OF AMERICA, INTERVENOR-DEFENDANT.

NOTICE OF MOTION

SIRS:

PLEASE TAKE NOTICE that upon the pleadings, the affidavit of John G. Brosnan, Esq., sworn to on August 21, 1975, the affidavit of James D. Martin, sworn to on August 21, 1975, the affidavit of Paul G. Dembling, Esq., sworn to August 25, 1975, the transcript of the deposition of Bristol Laboratories by Richard Cormier and the Rule 9(g) Statement and Supplemental Rule 9(g) Statement and upon all prior proceedings had herein, the intervenor-defendant, United States of America, will renew its motion for an order pursuant to Rule 56 of the Federal Rules of Civil Procedure awarding summary judgment to the United States for the relief prayed for in its counterclaim on the ground that there is no genuine issue as to any material fact and that the United States is entitled to judgment as a matter of law and for such other and further relief as the Court deems to be proper, before the Honorable Morris E. Lasker, on October 22, 1976 at 10:00 a.m. in the forenoon of that day in Room 2903, United States Courthouse, Foley Square, New York, New York.

Dated: New York, New York
October 1, 1976

ROBERT B. FISKE, JR.
United States Attorney for the Southern District of New York, Attorney for Defendants

By: /s/ _____
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UNITED STATES DISTRICT COURT
SOUTHERN DISTRICT OF NEW YORK

75 Civ. 1334 (MEL)

BRISTOL LABORATORIES DIVISION OF BRISTOL-MYERS COMPANY, PLAINTIFF,

-against-

ELMER B. STAATS, COMPTROLLER GENERAL OF THE UNITED STATES, DEFENDANT,

and

UNITED STATES OF AMERICA, INTERVENOR-DEFENDANT.

SUPPLEMENTAL STATEMENT UNDER LOCAL RULE 9(g)

SUPPLEMENTAL STATEMENT OF THE MATERIAL FACTS AS TO WHICH THERE ARE NO GENUINE ISSUES

The following is a supplemental statement of the material facts as to which defendants contend there is no genuine issue to be tried.

12. As a substitute for item 11 of the Rule 9(g) Statement, dated August 28, 1976, submitted by defendants the following:

> Plaintiff assigns standard direct manufacturing costs, standard manufacturing overhead, and royalty costs to individual products.

13. No costs of plaintiff are assigned exclusively to non-government contracts.

14. Plaintiff does on occasion allocate for internal purposes advertising and promotion costs, sales and market-

ing costs and research costs to individual products.

Dated: New York, New York
October 1, 1976

ROBERT B. FISKE, JR.
United States Attorney for the Southern District of New York, Attorney for Defendants.

By: /s/ _____
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UNITED STATES DISTRICT COURT
SOUTHERN DISTRICT OF NEW YORK

Civil Action No.
75 CIV 1334 (MEL)

BRISTOL LABORATORIES DIVISION OF BRISTOL-MYERS COMPANY, PLAINTIFF,

-against-

ELMER B. STAATS, COMPTROLLER GENERAL OF THE UNITED STATES, DEFENDANT,

and

UNITED STATES OF AMERICA, INTERVENOR-DEFENDANT.

NOTICE OF MOTION FOR SUMMARY JUDGMENT PURSUANT TO RULE 56, F.R.C.P

SIRS:

PLEASE TAKE NOTICE that upon the statement of material facts as to which there is no genuine issue to be tried; the affidavit of Gilbert H. Weil, dated July 22, 1975; the affidavit of Lorne C.D. Macbeth, dated September 29, 1975; the pleadings herein; defendant Staats's answers to plaintiff's first set on interrogatories; the transcript of the deposition of Bristol Laboratories by Richard J. Cormier; the memorandum in support of plaintiff's initial motion for summary judgment; the memorandum in opposition to intervenor-defendant's initial motion for summary judgment; plaintiff's supplemental statement under local Rule 9(g) and the accompanying memorandum, plaintiff will move this Court at Room 2903, United States Courthouse, Foley Square, New York, New York, on the 15th day of November, 1976, at ten o'clock in the forenoon, for an order that plaintiff is entitled to judgment as a matter of

law (1) limiting defendant Staats's access to an examination of plaintiff's books, documents, papers and records, in accordance with 10 U.S.C. § 2313(b) and 41 U.S.C. § 254(c) and various contracts between plaintiff and the United States, to those records which are directly pertinent to and involve transactions related to such contracts, (2) prohibiting defendant Staats from gaining access to and conducting examination of plaintiff's books, documents, papers or records which are pertinent to and involve transactions related only to contracts other than the aforesaid contracts and (3) dismissing intervenor-defendant's counterclaim except to the extent that it properly seeks access to and examination of those of plaintiffs books, documents, papers and records which are directly pertinent to and involve transactions related to the said government contracts.

The grounds for this motion are the same as those stated in plaintiff's notice of its initial motion for summary judgment, filed with this Court.

Dated: New York, New York
November 5, 1976

YOURS, ETC.
WEIL, GUTTMAN & DAVIS
/s/By: _____
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UNITED STATES DISTRICT COURT
SOUTHERN DISTRICT OF NEW YORK

75 CIV 1334 (MEL)

BRISTOL LABORATORIES DIVISION OF BRISTOL-MYERS COMPANY, PLAINTIFF,

-against-

ELMER B. STAATS, COMPTROLLER GENERAL OF THE UNITED STATES, DEFENDANT,

and

UNITED STATES OF AMERICA, INTERVENOR-DEFENDANT.

SUPPLEMENTAL STATEMENT UNDER LOCAL RULE 9(g)

SUPPLEMENTAL STATEMENT OF THE MATERIAL FACTS AS TO WHICH THERE ARE NO GENUINE ISSUES

The following is a supplemental statement of the material facts as to which plaintiff contends there is no genuine issue to be tried.

13. Plaintiff does not allocate or assign costs or expenses exclusively to government contracts.

14. Plaintiff does not allocate expenses for research and development, general and administrative or advertising and promotion.

15. For the limited purpose of use in reviewing employee compensation, plaintiff identifies some of its advertising and promotion expenses by product; however, such identification is not a factor in the negotiation with or the prices set to the government.

YOURS, ETC.
WEIL, GUTTMAN & DAVIS

/s/ _____
By: _____
ROBERT L. SHERMAN
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UNITED STATES DISTRICT COURT
SOUTHERN DISTRICT OF NEW YORK

75 Civ. 1334 (MEL)

BRISTOL LABORATORIES DIVISION OF BRISTOL-MYERS COMPANY, PLAINTIFF,

-against-

ELMER B. STAATS, COMPTROLLER GENERAL OF THE UNITED STATES, DEFENDANT,

and

UNITED STATES OF AMERICA, INTERVENOR-DEFENDANT.

PROTECTIVE ORDER ON CONSENT

This action having been remanded to this Court by the United States Court of Appeals for the Second Circuit for consideration of plaintiff's request for a protective order and without prejudice to the appeals of the parties and the parties having agreed to the entry of a protective order, it is now hereby

ORDERED, that every book report, paper, record, and other document (all hereinafter referred to as "document") designated as confidential by Bristol Laboratories Division of Bristol-Myers Company ("Bristol") or any of its divisions or subsidiaries and provided or otherwise made available to the Comptroller General or any of his successors, agents, employees, or subordinates (all hereinafter referred to as "the Comptroller General"), and every summary thereof and extract therefrom by whomever made, and all data and information contained therein, including any accountants' work papers (all hereinafter referred to as "data") shall be held in confidence and shall not be provided or otherwise made available by the Comp-

troller General to any person or agency outside the General Accounting Office except as provided in subparagraphs (a) and (b), below. No copies of Bristol's documents shall be included in accountants' work papers without the approval of Bristol.

Any document and data referred to in the above paragraph shall be used by the Comptrollor General solely for the purpose of a contract study. Upon completion of that study, the Comptroller General shall immediately return to Bristol all documents described in that paragraph. Any data in which Bristol, any of its divisions or subsidiaries, or any product manufactured or sold by any of them are or may be directly or indirectly identified which the Comptroller General deems it necessary to retain shall be retained by the General Accounting Office and deposited with and maintained by the Comptroller General under security measures to be agreed upon the the parties. Access to such data by any person shall be permitted only upon written authorization of the Comptroller General, and as limited in the subparagraphs following next denominated (a) and (b).

(a) Any of the data referred to in the above paragraph may be published, provided to, or otherwise made available to a person or agency outside the General Accounting Office if the data are published, provided, or made available so that any direct or indirect identification of Bristol, any of its divisions or subsidiaries, or any product manufactured or sold by any of them, is not reasonably possible. Bristol shall be afforded a reasonable opportunity to examine and offer its comments regarding any data considered for release, including any report issued by the Comptroller General that includes such data, before release of the data or report.

(b) The Comptroller General may comply without regard to the limitations of this Order set forth above, with an official written request for any of the data referred to above submitted to him by either House of Congress, or any committee of the House of Representatives or the Senate, or any joint committee of the two Houses to the

extent authorized and directed by law. The Comptroller General will cause prompt notice of any such request to be given to Bristol and to this Court at least seven calendar days prior to furnishing the data requested, and it is

FURTHER ORDERED, that the Comptroller General and the United States shall notify Bristol promptly of any request for disclosure, subpoena *duces tecum*, civil action, or other order or application for an order seeking production, release, or disclosure of any data referred to above, and further agree to use their best efforts to protect the confidentiality of such data, except as provided above, including resort to appropriate judicial remedies and cooperation with Bristol in such efforts, and it is

FURTHER ORDERED, that the Court shall retain jurisdiction to interpret and enforce the terms of this order, upon application of any party.

New York, New York
Sept. 6, 1979.

/s/ _____
H. MORRIS E. LASKER
United States District Judge

CONSENTED AND AGREED TO:

WEIL, GUTTMAN & DAVIS
Attorneys for Bristol Laboratories Division of Bristol-Myers Company

By: /s/ _____
ROBERT L. SHERMAN

ROBERT B. FISKE, JR.
Attorney for Elmer B. Staats, Comptroller General of the United States and the United States of America.

BY: /s/ _____
NAOMI REICE BUCHWALD
Assistant United States Attorney

Supreme Court of the United States

No. 80-264

ELMER B. STAATS, COMPTROLLER GENERAL OF UNITED STATES, ET AL., PETITIONERS,

v.

BRISTOL LABORATORIES DIVISION OF BRISTOL-MYERS COMPANY

ORDER ALLOWING CERTIORARI. Filed December 8, 1980

The petition herein for a writ of certiorari to the United States Court of Appeals for the Second Circuit is granted.

Justice Stewart took no part in the consideration or decision of this petition.

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Supreme Court, U. S.
FILED
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MICHAEL RODAK, JR., CLERK

No. 80-264

IN THE

Supreme Court of the United States

OCTOBER TERM, 1979

ELMER B. STAATS, COMPTROLLER GENERAL
OF THE UNITED STATES, AND
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v.

BRISTOL LABORATORIES DIVISION OF
BRISTOL-MYERS COMPANY

ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE SECOND CIRCUIT

BRIEF FOR RESPONDENT IN OPPOSITION

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BRIEF FOR RESPONDENT IN OPPOSITION

Statement

The government Petition states, at page 5, "[Bristol] also refused to provide 'records relating to the methodology and decisions involved in the firm's establishment of prices for the products purchased under the contracts' [C.A. App. 81]."

The language quoted was not Bristol's, but, rather, the Comptroller General's. Bristol, from the very beginning, has been willing to furnish records relating to such methodology and decisions regarding the prices to the government for the products purchased under *its* contracts. It refused

only with respect to prices to non-governmental purchasers. (C.A. App. 83)

ARGUMENT

I.

There is not such a conflict of law among the circuits as the government attempts to portray. (Petition, pp. 8-9.)

The difference in outcomes between, on the one hand, *Hewlett-Packard,*[1] *Lilly*[2] and *Abbott,*[3] and, on the other, the within case,[4] is rooted in the variant views of the respective courts as to facts they found to be determinative in their individual cases rather than in conflict concerning the law itself.

There would, as will be shown below, appear to be no disagreement among the circuits that "books, documents, papers, and records" reflecting components of a price charged the government by a contractor in a negotiated contract "involv[e] transactions related to such contracts" and, when "directly pertinent" to such price-determining factors, must be accessible by the Comptroller General pursuant to contracts under 10 U.S.C. 2313(b) and 41 U.S.C. 254(c). Conversely, there is no apparent inter-circuit disagreement that "transactions" which do not impact upon price or performance do not "relate to such contracts"; and that records of such unrelated transactions (whether

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[1] *Hewlett-Packard Co.* v. *United States,* 385 F.2d 1013 (9th Cir. 1967), *cert. denied,* 390 U.S. 988.

[2] *Eli Lilly & Co.* v. *Staats,* 574 F.2d 904 (7th Cir. 1978), *cert. denied,* 439 U.S. 959.

[3] *United States* v. *Abbott Laboratories,* 597 F.2d 672 (7th Cir. 1979).

[4] *Bristol Laboratories* v. *Staats,* 620 F.2d 17 (2d Cir. 1980).

or not "directly pertinent" to them) are not made accessible by the statutory and contractual provisions now under consideration. Even less, if possible, is there manifestation of any circuit deeming that in light of the qualifications "*directly* pertinent to" or "*directly* pertain to" (emphasis supplied) the Comptroller General is empowered to explore every book, document, paper, and record that is at all related to any and every cost going into any and every product manufactured by a firm that happens to have one or more supply contracts with the government.

In each of the Ninth and Seventh Circuit cases referred to above, the courts found *as fact* that the contractor's records at issue reflected elements entering into the prices charged the government. In the case at bar, to the contrary, the courts below have unanimously[5] found that the records denied to the Comptroller General contain no such data. It was upon that *factual* finding,[6] made by the courts below after the government had been given full opportunity to discover the nature of the withheld records,[7] that

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[5] "We affirm for the reasons given in Judge Lasker's excellent opinion . . . to which we refer the reader." (Petition, p. 3a)

[6] "The documents, affidavits and memoranda of law submitted by the parties establish that the controversy is not as much over the legal construction of the right-of-access clause in the contracts and statutes, as it is a factual dispute concerning Bristol's actual accounting and business procedures." (Memorandum of district court on cross motions for summary judgment, C.A. App. 20.)

[7] "Discovery is necessary to enable the government to inform itself as to Bristol's methods of accounting and allocation of costs * * * * [T]he proper course to follow is to restrict initial discovery by the Comptroller General (CG) to depositions of knowledgeable officers of Bristol Labs as to Bristol's methods and procedures for allocation of costs of all items not allocated exclusively to non-government contracts. No discovery shall be made of the books or accounts of Bristol Labs until termination of the depositions required above. Upon termination of such depositions the parties shall be free to move for such relief as appears justified." (*Idem*, C.A. App. 22-23.) The government did not move for any further discovery.

they concluded such books and records were not directly pertinent to transactions related to Bristol's contracts with the government[8] and that the government's contrary argument is such as to open virtually every income and expense related book, document, paper, and record of Bristol to the Comptroller General's perusal.[9]

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[8] "[The Comptroller General] is, of course, entitled to examine all 'directly pertinent records involving transactions related to the contract.' Although these words give general guidance, they do not provide answers to the specific questions which arise in the context of each case. We agree with the government that the issue should not depend entirely on a contractor's bookkeeping method, i.e., whether it does or does not assign particular costs to particular contracts or products. However, we do not understand this to be Bristol's contention. As set forth above, Bristol allocates only the direct cost of manufacture by product. These are among the costs it offers to make available, but they are by no means the limit of its offer. Rather, Bristol is willing to provide all records relating to manufacturing costs and the pricing of the products sold to the government. The specific list of items Bristol offers to make available, set forth at page 3, *supra*, appears to reflect a responsible and reasonable effort to distinguish 'directly pertinent' matter within the meaning of the access to records clause. It represents a sensible point at which to draw the line."(Petition, p. 12a.)

[9] "Bristol agrees that it is obliged by the terms of the contracts to provide access to records of its manufacturing costs, records which relate to the pricing of the products delivered and records required to verify all data obtained during the course of the review. Accordingly, Bristol states that it is ready and willing to allow GAO personnel to inspect its books and records with regard to the following items, which it lists as factors taken into account in setting prices to the government: manufacturing costs (including raw and packaging materials, labor and fringe benefits, quality control and supervision); manufacturing overhead (including plant administration, production planning, warehousing, utilities and security); royalty expenses; and delivery costs. However, it strenuously resists producing data with respect to research and development, marketing and promotion, distribution and administration (except to the extent that these areas may be included in the factors listed above), because it claims that these costs are too remote to the contracts and have only the most general relation, if any, to the prices charged.

"The United States insists that the GAO may inspect Bristol's records with respect to any and all costs met in whole or in part

With these as given facts—i.e., that the records sought do not pertain to factors entering into the contract prices, and the governmental search would extend to virtually all of Bristol's books and records[10]—there is no reason to believe, and the government has shown none, that either the Ninth or the Seventh Circuit would reach a different conclusion in a case presenting those facts than has the Second Circuit.

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from revenues earned on the federal contracts, whether or not those costs are specifically assigned by Bristol to the contracts or the products delivered. According to the government the test is simply 'whether the burden of [the] costs is borne by the Government in the prices it must pay for the contract items.' (Government's Memorandum, August 29, 1975 at 13)

"The Government's theory has far reaching implications. The only items excludable from the Comptroller General's reach would be those, if any, which relate to the costs recovered exclusively from non-government contracts. (Government's Memorandum, August 29, 1975 at 13) It is undisputed, however, that Bristol does not separately compute the cost of government and non-government contracts or pay for them out of separate funds. Accordingly, there are no excludable records under the Government's theory. Indeed, the company does not compute the costs attributable to any particular contract. It does allocate certain direct costs, for manufacturing and overhead, by product. Records of these expenses are thus readily available and are among those the company concedes to be discoverable. Its other expenses are not allocated at all; they are pooled and met out of gross revenues. In other words, revenues from government contracts are co-mingled with revenues from non-government contracts, and the resulting fund is used to pay for all expenses. If the government's interpretation of the access to records clause is correct, Bristol will be required to make available virtually all of its books and records, because although it is impossible to trace the use of government dollars, those dollars contribute to the fund from which all of the company's expenses are paid. (Petition, pp. 8a-10a.)

[10] These are the facts which, having been agreed upon by both courts below, this Court would accept if it granted the writ of certiorari petitioned for. *Branti* v. *Finkel*, —— U.S. ——, at ——, 100 S.Ct. 1287, at 1291 n.6 (1980); *Berenyi* v. *District Director, Immigration and Naturalization Service*, 385 U.S. 630, 670 (1967); *Graver Tank & Mfg. Co.* v. *Linde Air Products Co.*, 336 U.S. 271, 274-75 (1949).

In each of the other circuits' decisions upon which the government relies the facts patently were, or at least were deemed by the courts to be, that the transactions as to which books and records access was sought by the Comptroller General were such as to register their impact upon the prices to the government. Thus:

Hewlett-Packard (supra, p. 2) was embraced by *Lilly* (supra, p. 2) as a determinative precedent,[11] and consequently was carried forward as the genetically controlling source of the *Abbott* decision (infra, p. 8). However, a fair reading of *Hewlett-Packard* clearly indicates that the Ninth Circuit was not concerned with the Comptroller General's right to access a contractor's records of costs neither involved in negotiating nor incurred in fulfilling a government contract. Thus, the case presents no conflict with the one at bar and provides no basis for construing *Lilly* or *Abbott* as though they do.

To the extent that it may be relevant, *Hewlett-Packard* supports the Second Circuit for there the records to which the Comptroller General was given access were only those "relating to the cost of producing the items furnished by Hewlett-Packard Company under the aforesaid contracts, including costs of direct material, direct labor and overhead costs".[12] The Comptroller General was, accordingly, not permitted so expanded an examination of records as he seeks here, and the case is not authority for allowing it.

> Production costs directly pertain to that subject matter . . . Production costs involve transactions relating to the contract, because they encompass business arrangements made by the contractor in obtaining the materials, labor, facilities and the like required

[11] 574 F.2d at 912-13.

[12] 385 F.2d at 1016.

by it in fulfilling its commitment with reference to the subject matter of the contract. (385 F.2d at 1016.)

Lilly itself is in its holding conformant in the above respect with *Hewlett-Packard* and not in conflict with the Second Circuit. Its decision was based upon a factual conclusion that the records sought by the Comptroller General contained information as to costs that affected the prices charged the government. The *Lilly* court was convinced that as a matter of fact the research and development costs involved in that case "at the least appear to have a logical, causal and consequential relationship to a portion of the price of the products purchased by the Government." [13] Thus, the difference in result between *Lilly* and the courts below in this case is entirely accountable for by their variant views of the facts.

One may agree or disagree with the Seventh Circuit's factual determination,[14] one may maintain or dispute that

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[13] The court continued, "Further, contrary to plaintiff's contention, such costs are not 'remote' within the established definitions of that term in relation to at least a portion of the price because their inclusion of the price in the product is not unforeseeable once the costs are incurred, nor is their impact on a part of the price significantly altered by any intervening cause." (574 F.2d at 914.)

"[T]he district court need not grant access to any additional documents, and no information need be produced relating to classes of costs that have no more than a *de minimis* impact on the price of a product purchased by the Government." (*Idem* at 918.)

[14] There can be a variety of reasons why a contractor might be willing to negotiate a price, whether with the government or a private customer, that does not defray particular operational costs. Prestige might be one; establishing an initial contact and, hopefully, resultant good will with a potentially long term purchaser; reduction of down-time on manufacturing lines, thus ameliorating unproductive overhead; economies of scale in procuring raw materials as a result of the increased volume from the additional patronage. In any event, as mentioned above, the government had full opportunity through discovery in the within case to demon-

the Second Circuit's (and district court's) findings as to the facts herein should have been the same as those of the Seventh Circuit, but all of that is beside the present point. The oppositeness of their final rulings is a product of different factual perceptions, not of conflict as to substantive law. A mere difference in ultimate decisions of fact among separate courts, each based on its own, distinct, evidentiary record, does not present such a conflict as calls for review by this Court.[15]

Even if the *Lilly* determination were considered to be one of law, in conflict with a substantive conclusion by the Second Circuit herein, revisitation of *Lilly* in the light of *Abbott* and evaluation of their composite significance makes clear that such a postulated conflict no longer exists. The substantive stance that the government would attribute to *Lilly* would, from any realistic point of view, no longer be extant, if ever it was. Two of the three judges in *Abbott* made clear that they would have decided *Lilly* the other way, had they sat upon it; and they held as they did in *Abbott* only because of the constraint of *stare decisis*. (597 F.2d at 674-75.)

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strate, if it had been the true fact, that Bristol's withheld records contained information relating to transactions that did actually find their way into the prices set in the negotiated contracts herein or could reasonably have been expected to have done so (supra, p. 3).

[15] The Seventh Circuit's rulings with regard to the improper purpose of the Comptroller General, which occupied so much attention in *Lilly* (574 F.2d at 909-12) and *Abbott* (597 F.2d at 674-75) find no counterpart in the within case's issues or decisions to conflict with.

II.

The decision of the courts below is totally accordant with the legislative history of 10 U.S.C. 2313(b) and 4 U.S.C. 254(c). (Petition, pp. 10-17.)

The driving motivation of the congress was to empower the Comptroller General to audit governmental contracts' costs and performance to the end that the government be guarded against excessive cost or waste. The listing recited in the Petition resounds with that dominant, if not single-minded, purpose.

But, if Bristol's contracts with the government are not overpriced without taking into account its pool of research and development, advertising and promotion, distribution, and administration costs to offset its gross income from them, they certainly could not become so by introducing those costs. Quite the contrary.

If Bristol was satisfied to proffer no costs other than those enumerated at page 4, fn. 9 above, to justify the prices in the subject contracts, certainly no harm is done to the Comptroller General's responsibility and core interest to monitor the reasonableness of Bristol's prices to the government. Excluding cost items from the substantiation of prices can put only downward pressure on them to be fair.

Inquiry by the Comptroller General into such other, but unincluded, expenses would enhance but could not impugn the fairness of Bristol's prices. Without including those costs as justification, Bristol's prices stand in their poorest light for reasonableness. Adding them could only improve Bristol's appearances.

CONCLUSION

The petition for a writ of certiorari should be denied.

Respectfully submitted,

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Supreme Court, U.S.
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No. 80-264

In the Supreme Court of the United States

OCTOBER TERM, 1980

ELMER B. STAATS, COMPTROLLER GENERAL
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v.

BRISTOL LABORATORIES DIVISION OF
BRISTOL-MYERS COMPANY

ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE SECOND CIRCUIT

REPLY MEMORANDUM FOR THE PETITIONERS

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REPLY MEMORANDUM FOR THE PETITIONERS

---

1. Respondent does not contest the importance of a uniform interpretation of the statutory access-to-records provisions to the proper administration of the federal procurement system. Nor does respondent dispute that divergent constructions of these provisions by the courts of appeals would warrant this Court's review. See Pet. 9. Respondent does assert, however, that the decision below has not created a conflict among the circuits because, in its view, the courts' holdings can be reconciled in terms of the different facts presented in each case. Respondent contends that these differences in outcome turn not on disagreements over the governing legal principles but rather on the application of those principles to the distinct factual records under consideration.

Respondent's reading of these cases is unfounded. As discussed in the petition (Pet. 8-9 & n.9), there is a clear conflict in the circuits concerning the construction of the access-to-records provisions.[1] Indeed, contrary to respondent's argument, the courts of appeals themselves have expressly recognized the existence of this conflict (see Pet. 8); as the Second Circuit observed in adopting the opinion of the district court in this case, the Seventh Circuit's decisions in *United States* v. *Abbott Laboratories*, 597 F. 2d 672 (1979), and *Eli Lilly & Co.* v. *Staats*, 574 F. 2d 904, cert. denied, 439 U.S. 959 (1978), "reject the holding of the * * * [district court], but we do not find their reasoning persuasive" (Pet. App. 3a).[2]

Moreover, the facts in this case and in *Eli Lilly* do not differ in any material regards.[3] Both of these cases involve

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[1]See also Br. in Opp. 6 n.4, *SmithKline Corp.* v. *Staats*, conditional petition for cert. before judgment pending, No. 80-434 (filed Sept. 18, 1980). We are providing respondent with a copy of our brief in opposition in *SmithKline*.

[2]Respondent attempted in the court of appeals to distinguish *Eli Lilly* on the same factual grounds it advances here (Bristol Br. 16-19), but the Second Circuit declined to adopt this argument, concluding instead that its decision and *Eli Lilly* were squarely in conflict (Pet. App. 3a).

[3]An affidavit filed in the district court in this case, which was not challenged by respondent, stated GAO's understanding (1) that the several pharmaceutical companies in question, including respondent, utilized substantially similar cost accounting systems that only assigned certain manufacturing costs to individual products but treated all other costs on an unallocated basis, and (2) that the companies recovered their costs, both allocated and unallocated, from general revenues that included payments by the government under the contracts at issue (C.A. App. 106-107). See also *United States* v. *Abbott Laboratories*, *supra*, 597 F. 2d at 673-674, 675; *SmithKline Corp.* v. *Staats*, 483 F. Supp. 712, 715, 720, 721 n.7, 722 (E.D. Pa. 1980), appeal pending, No. 80-1464 (3d Cir., filed Mar. 19, 1980), conditional petition for cert. before judgment pending, No. 80-

negotiated fixed-price contracts for the sale of pharmaceutical products (see Pet. 3-4; 574 F. 2d at 907, 920, 925). In each of the cases the price charged the government was based on the company's standard price for its commercial customers, and there was no discussion of costs at the time the contracts were executed (see Pet. 12 n.14; 574 F. 2d at 906, 907, 914, 920, 923, 925). Neither of the contractors allocated, on either a product or a customer basis, many of the costs that were the subject of the Comptroller General's request for access to records, and neither of them purported to have directly or specifically considered these costs in setting their prices (see Pet. 5-6, 12 & n.13; 574 F. 2d at 914, 920, 925).[4] In both cases the revenues derived from the government contracts were used, as part of commingled general revenues, to defray all costs and expenses, including the unallocated costs reflected in the records sought by GAO (see Pet. 6-7, 12; C.A. App. 160a-165a, 168a-169a; *Eli*

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434 (filed Sept. 18, 1980); *Merck & Co.* v. *Staats*, Civil Action No. 74-1447 (D.D.C. Aug. 12, 1977), slip op. 1-3, appeals pending, Nos. 79-1435, 79-1438 (D.C. Cir., argued Feb. 11, 1980), conditional petition for cert. before judgment pending, No. 80-416 (filed Sept. 16, 1980); cf. *Hewlett-Packard Co.* v. *United States*, 385 F. 2d 1013, 1014, 1016 (9th Cir. 1967), cert. denied, 390 U.S. 988 (1968).

[4]Respondent characterizes (Br. in Opp. 7) the *Eli Lilly* holding as resting on the court's finding "that as a matter of fact the research and development costs involved in that case 'at the least appear to have a logical, causal and consequential relationship to a portion of the price of the products purchased by the Government' " (quoting 574 F. 2d at 914). We submit that respondent has misconstrued the court's reasoning in *Eli Lilly*. The Seventh Circuit's opinion makes evident that the above-quoted passage refers not to the particular facts of record in that case but rather to "[t]he [m]eaning of the [s]tatutes * * * as applied to the pharmaceutical industry * * *" (574 F. 2d at 913). The court's legal analysis of the access-to-records provisions and its application of those provisions based on the nature of the pharmaceutical industry are equally apposite to the case at bar.

Lilly & Co. v. *Staats*, *supra*).[5] Finally, GAO's requests for access to the specified records of the pharmaceutical companies were identical in each case (see Pet. 4, 8; 574 F. 2d at 906).

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[5]The depositions of company officials made clear that Eli Lilly, like respondent, recovered all of its costs, including its unallocated costs, from commingled general revenues that consisted in part of payments by the government:

Q. [government attorney] * * * So, is it correct to assume that Lilly, as a profitable company, recovers all of its costs through the sale or revenues derived from the sale of its products?

A. [Eugene L. Step, President, Pharmaceutical Division, Eli Lilly & Co.] Sure. I think that the financial statements are very specific testimony to that fact.

Q. Quite impressive, as a matter of fact.

Well, from that, then, would you conclude that your research and development costs, your general and administrative costs, your marketing costs, and your manufacturing costs are recovered through the sale, revenues derived from the sale of the pharmaceutical products?

A. I think that's fair. All costs of doing business are recovered from the sale, from the revenues derived from the sale of all of our products. That includes our pharmaceutical products, our agricultural products, our cosmetics, certain packaging products we sell.

* * * * *

A. * * * I view the Federal Government as a customer like any other. * * *

In other words, it is of no more interest to me what the standard cost of a product is in quoting to the Federal Government than it is in putting it in the price list. I'm not there to turn over dollars. I'm not there to recover standard costs in sales to the Federal Government. I'm there to earn a profit on those sales, and if we're down to a price that's so close to standard that the question is recovering costs, we won't bid. I'm not interested in that business. We'll let some of our competitors have that.

Q. I think I understand what you're saying. So, that if a situation should develop that the price quoted to the Government would

On these common facts, the Seventh Circuit has sustained the Comptroller General's authority to inspect the designated records of unallocated costs; the Second

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Q.—Continued:

recover only your standard costs or close, that is not the kind of business that you would be interested in capturing?

A. That's right.

* * * * *

Q. If your quoted price in the situation that we have just discussed would recover only your manufacuturing costs, or slightly in excess of it, isn't it fair to say that you wouldn't be interested in that business because such a price wouldn't recover your other costs?—your research and development cost, your general and administration cost, your marketing cost.

A. Well, you're getting there. You are getting to a kind of a convoluted way of what I'm really saying, is that we follow the prices. We have people who follow the prices at which the Government lets tenders, or on which the Government awards tenders. If the Government wants to buy penicillin VK; they put out a tender. The results of those are advertised, so we know what the going market is. If that going market is attractive to us, we would bid. If the going market is not attractive to us, we wouldn't bid.

* * * * *

Q. Are the revenues derived from sales to the Government placed in any special bank account?

A. [Deane Pinney, Administrator for the Financial Reporting, Eli Lilly & Co.] No.

Q. Are they commingled with other revenues?

A. Yes.

Q. Are revenues then derived from the sale of the company's products, including revenues derived from sales to the Government, used to recover the costs of those sales?

A. Yes.

C.A. App. 161a, 163a-164a, 165a, 169a, *Eli Lilly & Co.* v. *Staats*, *supra*.

Circuit has reached exactly the opposite conclusion and prohibited the requested inspection.[6] Thus, there is an unavoidable conflict that should be resolved by this Court.[7]

2. Respondent also briefly adverts (Br. in Opp. 9) to the merits of the issue presented in this case and contends that the decision below is consistent with the legislative history of the access-to-records statutes. In agreement with our position (Pet. 10-13),[8] respondent concedes (Br. in Opp. 9) that the purpose of the statutes "was to empower the Comptroller General to audit governmental contracts' costs and performance *to the end that the government be guarded against excessive cost or waste*" (emphasis added).[9] Especially in the pharmaceutical

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[6]Respondent quotes at some length (Br. in Opp. 3 nn.6, 7) from the district court's opinion initially denying cross-motions for summary judgment on the ground that the record did not adequately reveal respondent's "methods of accounting and allocation of costs" (C.A. App. 22). At the present stage, however, these factual uncertainties have been clarified, summary judgment has been entered against the government, and the petition raises a legal issue that does not depend on any outstanding factual disputes between the parties (see Pet. App. 6a n.1).

[7]Contrary to respondent's suggestion (Br. in Opp. 8), the fact that *Abbott* was decided on grounds of *stare decisis* in light of the decision by the same circuit court of appeals in *Eli Lilly* emphasizes rather than negates or minimizes the existence of a conflict between the Second and Seventh Circuits. We also note that the Seventh Circuit denied a petition for rehearing en banc in *Eli Lilly* (see 574 F. 2d 904).

[8]See also Comment, *The Comptroller General's Authority to Examine the Private Business Records of Government Contractors: Eli Lilly & Co.* v. *Staats*, 92 Harv. L. Rev. 1148, 1157-1158 & nn.67-68 (1979).

[9]Respondent has not addressed our further arguments (Pet. 14-17) that, because GAO's longstanding and consistent construction of the access-to-records provisions is reasonable and has not been

industry, where the direct costs of manufacturing and delivering individual products constitute as little as 9% of the sales price and manufacturers devote approximately 12% of sales revenues to unallocated research and development costs (see Pet. 13), the access-to-records provisions would afford a wholly inadequate protection against waste, excessive prices, and ineffective procurement if it is held, as the court below did, that the statutes do not extend to the companies' substantial unallocated costs pertaining to research and development, advertising and promotion, distribution, and administration. Rather, because Congress intended the Comptroller General to have "the proper tools to do the job the Congress has instructed him to do" (97 Cong. Rec. 13198 (1951) (remarks of Rep. Hardy)) and sought to enable him to determine whether the contract price was "extravagan[t]," "excessive," or "wasteful[]" (*ibid.*), we submit that the access-to-records provisions are applicable to the records of unallocated costs that have been requested by GAO in this case.[10]

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overturned by Congress, the court below erred in rejecting the interpretation of the statutes adopted by the agency charged with the responsibility for their administration.

[10]Respondent contends (Br. in Opp. 9; see also *id.* at 7-8 n.14) that the exclusion of its unallocated costs from consideration by GAO would necessarily work to the company's disadvantage in assessing the reasonableness of the contract price to the government. However, respondent does not assert that it priced its products on the basis of partial or incremental costs and, since the government was charged respondent's normal wholesale price (see Pet. 12 n.14), any contention that the contract price could be reasonable without regard to significant unallocated costs, such as research and development, is specious. At all events, respondent's position, even if correct in terms of the reasonableness of a specific contract, focuses solely on GAO's function to determine whether the individual "contract may have been an inappropriate means of meeting this

For the foregoing reasons and the reasons stated in the petition, it is therefore respectfully submitted that the petition for a writ of certiorari should be granted.

WADE H. MCCREE, JR.
Solicitor General

NOVEMBER 1980

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particular procurement need of the Government" and ignores its responsibility to study and recommend "the use of other methods of meeting future procurement needs." *Hewlett-Packard Co.* v. *United States*, *supra*, 385 F. 2d at 1016.

DOJ-1980-11

No. 80-264

In the Supreme Court of the United States

OCTOBER TERM, 1980

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AND

UNITED STATES OF AMERICA, PETITIONERS

v.

BRISTOL LABORATORIES DIVISION OF BRISTOL-MYERS COMPANY

ON WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE SECOND CIRCUIT

BRIEF FOR THE PETITIONERS

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BRIEF FOR THE PETITIONERS

QUESTION PRESENTED

Whether, with respect to negotiated government contracts, the Comptroller General is authorized by law to examine the contractor's books and records pertaining to costs of research and development, advertising and promotion, distribution, and administration, where such costs, although not allocated by the contractor to particular products or calculated on a product basis in determining price, are defrayed by the contractor from commingled general revenues that include the government's payments under the contracts.

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OPINIONS BELOW

The opinion of the court of appeals (Pet. App. 1a-4a) is reported at 620 F.2d 17. The opinion of the district court (Pet. App. 5a-12a) is reported at 428 F. Supp. 1388.

JURISDICTION

The judgment of the court of appeals was entered on March 25, 1980 (Pet. App. 13a-14a). On June 12, 1980, Mr. Justice Marshall extended the time for filing a petition for a writ of certiorari to and including August 22, 1980. The petition for a writ of certiorari was filed on August 21, 1980, and was granted on December 8, 1980 (J.A. 154). The jurisdiction of this Court rests upon 28 U.S.C. 1254(1).

STATUTES INVOLVED

1. 10 U.S.C. 2313(b) provides:

> Except as provided in subsection (c), each contract negotiated under this chapter shall provide that the Comptroller General and his representatives are entitled, until the expiration of three years after final payment, to examine any books, documents, papers, or records of the contractor, or any of his subcontractors, that directly pertain to, and involve transactions relating to, the contract or subcontract.

2. 41 U.S.C. 254(c) provides:

> All contracts negotiated without advertising pursuant to authority contained in this Act shall include a clause to the effect that the Comptroller General of the United States or any of his duly authorized representatives shall until the expira-

tion of three years after final payment have access to and the right to examine any directly pertinent books, documents, papers, and records of the contractor or any of his subcontractors engaged in the performance of and involving transactions related to such contracts or subcontracts. Under regulations to be prescribed by the Administrator, however, such clause may be omitted from contracts with foreign contractors or foreign subcontractors if the agency head determines, with the concurrence of the Comptroller General of the United States or his designee, that the omission will serve the best interests of the United States. However, the concurrence of the Comptroller General of the United States or his designee is not required for the omission of such clause—

(1) where the contractor or subcontractor is a foreign government or agency thereof or is precluded by the laws of the country involved from making its books, documents, papers, or records available for examination; and

(2) where the agency head determines, after taking into account the price and availability of the property or services from United States sources, that the public interest would be best served by the omission of the clause.

If the clause is omitted based on a determination under clause (2) a written report shall be furnished to the Congress. The power of the agency head to make the determination specified in the preceding sentences shall not be delegable.

STATEMENT

1. In 1973 and 1974, respondent Bristol Laboratories entered into three contracts with the Defense Supply Agency of the Department of Defense and one contract with the Veterans Administration for the sale of pharmaceutical products to the government. All four were negotiated fixed-price contracts, with a total price of approximately $2 million (Pet. App. 6a-7a; J.A. 88-93).[1] As required by 10 U.S.C.

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[1] A negotiated government contract is a method of procurement authorized by statute to be used in situations in which the formal public advertising and bidding procedure is deemed impractical or unnecessary. See 10 U.S.C. 2304(a); 41 U.S.C. 252(c). Respondent's VA contract was executed (J.A. 29, 89) pursuant to 41 U.S.C. 252(c)(10), which authorizes contracts to be negotiated without formal advertising "if * * * for property or services for which it is impracticable to secure competition"; each of respondent's contracts with the Defense Supply Agency was executed (J.A. 29-30, 90-91) under 10 U.S.C. 2304(a)(7), which provides that a contract may be negotiated without formal advertising "if * * * the purchase or contract is for medicine or medical supplies." For a general discussion of negotiated and fixed-price contracts, see, *e.g.*, I R. Nash & J. Cibinic, *Federal Procurement Law* 317-321, 412-415 (3d ed. 1977).

Negotiated contracts comprise approximately 90% of the total amount expended by the government for procurement. See I R. Nash & J. Cibinic, *supra*, at 317; see also F. Mosher, *The GAO: The Quest for Accountability in American Government* 318 (1979). In fiscal year 1979, the aggregate value of negotiated government contracts was approximately $78 billion. See Office of the Secretary of Defense, *Military Prime Contract Awards for Fiscal Year 1979*, Table 9 (1979); General Services Administration, *Procurement by Civilian Executive Agencies for Fiscal Year 1979*, Part I (1979).

2313(b)[2] and 41 U.S.C. 254(c),[3] each of the contracts contained a standard access-to-records provision in which respondent agreed that "the Comptroller General of the United States or any of his duly authorized representatives shall, until the expiration of three years after final payment under this contract * * *, have access to and the right to examine any directly pertinent books, documents, papers, and records of the Contractor involving transactions related to this contract" (Pet. App. 6a-7a; J.A. 89-93).

Pursuant to these statutory and contractual provisions, the Comptroller General, by letter of August 26, 1974, made a timely request to respondent for access to

> all books, documents, papers and other records directly pertinent to the contracts, which include, but are not limited to (1) records of experienced costs including costs of direct materials, direct labor, overhead, and other pertinent corporate costs, (2) support for prices charged to the Government, and (3) such other information as may be necessary for us to review the reasonableness of the contract prices and the adequacy of the protection afforded the Government's interests.

Pet. App. 7a-8a; J.A. 57-59. The Comptroller General explained that "because of the increasing Federal involvement in the procurement of pharmaceuticals, the General Accounting Office has underway a review

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[2] This provision is applicable to the Defense Supply Agency contracts.

[3] This provision is applicable to the Veterans Administration contract.

of the procurement of drugs by agencies of the Federal Government" and that the requested records were "necessary to conduct such a review" (J.A. 57).[4]

In reply, respondent offered to make available "(1) Bristol's contract files which included shipment and invoice records, (2) records and data relating to manufacturing costs assigned by the firm to the products purchased under the contracts, and (3) Bristol's product prices to its non-Federal customers" (J.A. 68). However, respondent declined to produce "records concerning costs incurred for activities such as research and development, marketing and promotion, distribution and administration * * * [because] such costs are not assigned to individual products and records concerning these costs are not pertinent to the cited contracts" (J.A. 69). Respondent also refused to provide "records relating to the methodology and decisions involved in the firm's establishment of prices for the products purchased under the contracts" (*ibid.*). By letter dated March 6, 1975, the Comptroller General advised respondent that its proposal failed to satisfy the legal requirements under which the GAO request had been made (J.A. 68-69).

2. On March 18, 1975, respondent commenced the present action in the United States District Court for the Southern District of New York seeking declaratory and injunctive relief against the Comp-

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[4] In an attachment to this letter, the Comptroller General further stated that "the clear intent of the statute was to provide for the examination by our Office of such of the contractor's records as would permit a valid evaluation of the reasonableness of the prices charged" (J.A. 63).

troller General (J.A. 11-13). The United States later intervened as a defendant and filed a counterclaim to gain access to the records requested by the Comptroller General (J.A. 27-34).

Respondent conceded in the district court that it was obligated "to provide access to records of its manufacturing costs, records which relate to the pricing of the products delivered and records required to verify all data obtained during the course of the review" (Pet. App. 8a). On this basis, it agreed to allow inspection of records pertaining to "the following items, which it lists as factors taken into account in setting prices to the government: manufacturing costs (including raw and packaging materials, labor and fringe benefits, quality control and supervision); manufacturing overhead (including plant administration, production planning, warehousing, utilities and security); royalty expenses; and delivery costs" (*ibid.*). However, respondent "strenuously resist[ed] producing data with respect to research and development, marketing and promotion, distribution and administration * * *" on the ground that these costs, which respondent neither allocated to particular products or contracts nor considered in setting the price charged to the government, "are too remote to the contracts and have only the most general relation, if any, to the prices charged" (*id.* at 8a-9a).

Following discovery, the district court granted respondent's motion for summary judgment and denied the cross-motion of the government (Pet. App. 5a-12a).[5] The court rejected the government's argu-

[5] The parties' initial motions for summary judgment were denied because of uncertainties concerning respondent's accounting methods (Pet. App. 6a n.1; J.A. 6-10). These cross-motions were renewed after completion of the necessary discovery.

ment that, with respect to respondent's unallocated costs, the access-to-records provision authorized examination of "all costs met in whole or in part from revenues earned on the federal contracts * * *" (Pet. App. 9a). Since respondent's unallocated costs "are pooled and met out of gross revenues * * * [consisting of] revenues from government contracts * * * com[m]ingled with revenues from non-government contracts," the court expressed its concern that the position urged by the government would mean that "there are no excludable records" and that respondent would be required "to make available virtually all of its books and records * * * because * * * government dollars * * * contribute to the fund from which all of the company's expenses are paid" (*id.* at 9a-10a). The court concluded that such a result would be "inconsistent" with the "words of limitation" in the access-to-records provisions authorizing the Comptroller General to examine " 'directly pertinent * * * records * * * involving transactions related to [the] contract' " (*id.* at 10a; emphasis omitted). In the court's view, the "reasonable assumption is that if Congress had wished to condition the receipt of a fixed-price negotiated contract on the contractor's agreement to allow such unusual and unfettered government inspection of their business records, it would have done so explicitly" (*ibid.*). In addition, the court held as a matter of contract law that "[t]he government's position is particularly unrealistic" because, in construing "the intent and understanding of the parties * * *, [i]t is inconceivable that [respondent], or any contracting firm, could have understood this clause to authorize the sweeping power of inspection claimed by the GAO" (*id.* at 10a-11a). Accordingly, the court sustained respondent's posi-

tion as "a responsible and reasonable effort to distinguish 'directly pertinent' matter within the meaning of the access to records clause. It represents a sensible point at which to draw the line" (*id.* at 12a).

3. On the government's appeal, the court of appeals affirmed in a per curiam opinion for the reasons given by the district court (Pet. App. 1a-4a).[6] The court of appeals also noted that two intervening decisions of the Seventh Circuit had "reject[ed] the holding of the court below," but it did "not find their reasoning persuasive" (*id.* at 3a). See *Eli Lilly & Co.* v. *Staats*, 574 F.2d 904 (7th Cir.), cert. denied, 439 U.S. 959 (1978); *United States* v. *Abbott Laboratories*, 597 F.2d 672 (7th Cir. 1979).

SUMMARY OF ARGUMENT

The General Accounting Office is charged by Congress with the responsibility to "investigate * * * all matters relating to the receipt, disbursement, and application of public funds * * * [and to] make recommendations looking to greater economy or efficiency in public expenditures." 31 U.S.C. 53(a). Pursuant to 10 U.S.C. 2313(b) and 41 U.S.C. 254(c), the Comptroller General is entitled to have access to, and to examine, the books and records of a government contractor that are directly pertinent to the contract and involve transactions relating thereto. Respondent acknowledges that the access-to-records provisions au-

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[6] After both parties had initially appealed, the court of appeals remanded the case for consideration of respondent's request for a protective order. Upon the consent of the parties, the district court approved a protective order on September 6, 1979 (Pet. App. 3a n.2; J.A. 151-153). Thereafter, only the government pursued its appeal. Our petition in this case raises no issue concerning the need for or scope of an appropriate protective order.

thorize the Comptroller General to inspect certain of its cost records, but it contends that the Comptroller General is not empowered to examine its records pertaining to unallocated costs of research and development, advertising and promotion, distribution, and administration. This contention is contrary both to the purpose and legislative history of the access-to-records statutes and to GAO's consistent and long-standing interpretation that Congress has not disapproved.

Sections 2313(b) and 254(c) are premised on Congress' determination that "negotiated contracts * * * require close supervision and control * * *." H.R. Rep. No. 791, 82d Cong., 1st Sess. 2 (1951). Representative Hardy, the sponsor of the legislation and chairman of the subcommittee that considered the bill, explained that examination of contractors' records by the Comptroller General would allow "the General Accounting Office to look behind the * * * [price] which had been established * * * [to assess whether it was] excessive" and would act as a "safeguard against waste and extravagance" in government procurement. 97 Cong. Rec. 13198 (1951). Because of its concern that "there is every chance in the world that the Government will come out on the short end of the deal," Congress enacted the access-to-records statutes to "enable the * * * [Comptroller General] to check the transaction, both from the Government records and the contractors' books" (*ibid.*) (remarks of Rep. Hardy). And, in light of GAO's responsibility to investigate and make recommendations regarding economy and efficiency in public expenditures, Congress intended that "the Comptroller General [be given] the proper tools to do the job the Congress has instructed him to do" and that, "if * * * [GAO] should find that the * * * [price

was] excessive, it could, and undoubtedly would, bring the facts to the attention of the contracting officer, and possibly in an extreme case, it might call attention of the Congress to the situation" (*ibid.*) (remarks of Rep. Hardy).

Moreover, GAO has consistently construed the access-to-records statutes to authorize examination of all cost records relating to the reasonableness of the contract price. On several occasions GAO has presented this interpretation to Congress, which has never indicated its disapproval.

The court of appeals, in sustaining respondent's position, ignored the purpose and legislative history of the access statutes and rejected this longstanding and consistent administrative construction. But as this Court has observed, the "objective * * * [in construing a statute] is to ascertain the congressional intent and give effect to the legislative will." *Philbrook* v. *Glodgett*, 421 U.S. 707, 713 (1975). Furthermore, it is a " 'venerable principle that the construction of a statute by those charged with its execution should be followed unless there are compelling indications that it is wrong * * *.' " *E. I. du Pont de Nemours & Co.* v. *Collins*, 432 U.S. 46, 54-55 (1977), quoting *Red Lion Broadcasting Co.* v. *FCC*, 395 U.S. 367, 381 (1969). And judicial deference to the agency's construction is especially appropriate where, as in this case, that "construction has been 'fully brought to the attention of the public and the Congress,' and the latter has not sought to alter that interpretation * * *." *United States* v. *Rutherford*, 442 U.S. 544, 554 n.10 (1979), quoting *Apex Hosiery Co.* v. *Leader*, 310 U.S. 469, 489 (1940).

In light of the language, legislative history, and evident purpose of the access-to-records provisions, the Comptroller General must be allowed to examine

all of the contractor's cost records that are necessary and appropriate to determine whether the price charged the government was "extravagan[t]," "excessive," or "wasteful[]." 97 Cong. Rec. 13198 (1951) (remarks of Rep. Hardy). Applying this standard to the present case, it is clear that the Comptroller General is entitled to access to respondent's cost records pertaining to research and development, advertising and promotion, distribution, and administration.

The court below denied access by GAO because the records in question involve costs that respondent neither allocates to particular products or contracts nor calculates on a product basis in setting prices. But the government cannot be bound by the accounting method respondent has established for its own purposes. If respondent had fully allocated its costs, GAO's right to conduct an inspection adequate to evaluate the reasonableness of the contract price would be clear, and no different outcome is warranted simply because respondent has chosen to allocate only some of its costs.

Respondent's election to keep its business records on the basis of unallocated costs cannot obscure the fact that an examination of those costs is necessary for the Comptroller General to fulfill his statutory function of determining whether the government has been charged a reasonable price. To operate profitably, respondent must recover its costs from sales revenues, and it uses the payments by the government under the contracts at issue, as part of commingled general revenues, to help defray its unallocated expenses. Accordingly, respondent's unallocated costs are critical to an assessment of the fairness of the contract price and the advisability of continued adherence by the government to the negotiated procurement methods employed here. Es-

pecially where, as in the pharmaceutical industry, direct manufacturing and delivery costs constitute only about 9% of a product's sale price, and manufacturers expend approximately 12% of sales revenues on research and development, it would completely frustrate GAO's inquiry into the appropriateness of the contract price to limit its examination to allocated costs such as production and delivery and to exclude such significant unallocated costs as research and development, advertising and promotion, distribution, and administration.

ARGUMENT

THE ACCESS-TO-RECORDS PROVISIONS AUTHORIZE THE COMPTROLLER GENERAL TO EXAMINE A CONTRACTOR'S BOOKS AND RECORDS PERTAINING TO UNALLOCATED COSTS DEFRAYED FROM COMMINGLED GENERAL REVENUES THAT INCLUDE THE GOVERNMENT'S PAYMENTS UNDER THE CONTRACT

A. Introduction

The General Accounting Office was established by the Budget and Accounting Act of 1921, ch. 18, Title III, Section 301, 42 Stat. 23, 31 U.S.C. 41. The GAO is "independent of the executive departments and under the control and direction of the Comptroller General of the United States" (31 U.S.C. 41), who is "appointed by the President with the advice and consent of the Senate" (31 U.S.C. 42) and serves for a term of 15 years subject to removal for cause "at any time by joint resolution of Congress" (31 U.S.C. 43). See also 5 U.S.C. 902; 31 U.S.C. 65(d). Thus, the GAO is "an independent agency within the legislative branch of the Government." I R. Nash & J. Cibinic, *Federal Procurement Law* 19 (3d ed. 1977). See also Cibinic &

Lasken, *The Comptroller General and Government Contracts*, 38 Geo. Wash. L. Rev. 349, 349 & nn.2, 3 (1970).

Among other duties, the Comptroller General "shall investigate * * * all matters relating to the receipt, disbursement, and application of public funds" and "shall make recommendations [to Congress] looking to greater economy or efficiency in public expenditures" (31 U.S.C. 53(a)). In addition, "[t]he Comptroller General is authorized and directed to make an expenditure analysis of each agency in the executive branch of the Government * * * which * * * will enable Congress to determine whether public funds have been economically and efficiently administered and expended" (31 U.S.C. 60). See also 31 U.S.C. 65(a) ("[t]he accounting of the Government [shall] provide * * * effective control over income, expenditures, funds, property, and other assets").

The access-to-records provisions at issue in this case—10 U.S.C. 2313(b) and 41 U.S.C. 254(c)—complement the foregoing statutes and specifically contemplate GAO review of contractors' books and records. See Cibinic & Lasken, *supra*, 38 Geo. Wash. L. Rev. at 388. By the express terms of Sections 2313(b) and 254(c), all government contracts negotiated pursuant to designated statutory authority must provide that the Comptroller General shall have access to, and be entitled to examine, the books and records of the contractor that are directly pertinent to the contract and involve transactions relating thereto. Respondent acknowledges that it is obligated to allow the Comptroller General to inspect certain of its cost records. See Pet. App. 8a; Br. in Opp. 4 n.9. See also *United States* v. *Abbott Laboratories*, 597 F.2d 672 (7th Cir. 1979); *Eli Lilly & Co.* v. *Staats*, 574 F.2d 904, 912-916 (7th Cir.), cert. denied, 439

U.S. 959 (1978); *Hewlett-Packard Co.* v. *United States*, 385 F.2d 1013, 1016 (9th Cir. 1967), cert. denied, 390 U.S. 988 (1968); *SmithKline Corp.* v. *Staats*, 483 F. Supp. 712, 722 (E.D. Pa. 1980), appeal pending, No. 80-1464 (3d Cir., filed Mar. 19, 1980), conditional petition for cert. before judgment denied, No. 80-434 (Dec. 8, 1980);[7] *Merck & Co.* v. *Staats*, Civ. Action No. 74-1447 (D.D.C. Aug. 12, 1977), slip op. 3-4, appeals pending, Nos. 79-1435, 79-1438 (D.C. Cir., argued Feb. 11, 1980), conditional petition for cert. before judgment denied, No. 80-416 (Dec. 8, 1980).[8]

Respondent contends, however, that the access-to-records provisions do not extend to records pertaining to its unallocated costs of research and development, advertising and promotion, distribution, and administration, despite the fact that these costs are defrayed from total revenues that include the government's payments under the contracts. In sustaining respondent's position, the court of appeals failed to consider the purpose and legislative history of the statutory provisions and to defer to GAO's longstanding and consistent interpretation that has been recognized and left undisturbed by Congress. Contrary to the court of appeals' decision, respondent's construction is inconsistent with the statutes and, if adopted by this Court, would severely hinder the Comptroller General's authority to promote sound government

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[7] Oral argument in *SmithKline* is currently scheduled for February 23, 1981. A motion of SmithKline, consented to by the government, to postpone the argument pending this Court's disposition of the instant case is pending before the Third Circuit.

[8] By order filed December 17, 1980, the District of Columbia Circuit, acting on its own motion, deferred decision in *Merck* pending a decision by this Court in the present case.

procurement practices. Indeed, in this case, because unallocated costs represent the predominant part of the price of pharmaceuticals sold to the government, the decision below would render meaningless the Comptroller General's right of access and would totally defeat his statutory responsibility to evaluate the fairness of the contract price.

B. GAO's Interpretation Is Consistent With The Legislative History Of The Access-To-Records Statutes And Furthers The Congressional Purpose

Contrary to the decision below, the legislative history of the access-to-records statutes makes clear that Congress intended the Comptroller General to have a broad right of access in order to determine the reasonableness of the contract price and the adequacy of the protection afforded the government in negotiated procurements. The access statutes were enacted in 1951 as amendments to the Armed Services Procurement Act of 1947, ch. 65, 62 Stat. 21 *et seq.*, and the Federal Property and Administrative Services Act of 1949, ch. 288, 63 Stat. 377 *et seq.* See Act of Oct. 31, 1951, ch. 652, 65 Stat. 700.[9] The Committee Reports expressed Congress' determination that "negotiated contracts * * * require close supervision and control * * *." H.R. Rep. No. 791, 82d Cong., 1st Sess. 2 (1951); S. Rep. No. 603, 82d Cong., 1st Sess. 2 (1951). Representative Hardy, the sponsor of the legislation and chairman of the subcommittee that

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[9] As originally enacted, the two statutory provisions were identical. Although the language of 10 U.S.C. 2313(b) was slightly altered in a subsequent recodification, no change of substance was intended. See Act of Aug. 10, 1956, ch. 1041, Section 49(a), 70A Stat. 640; 102 Cong. Rec. 13952 (1956) (statement of Sen. O'Mahoney).

considered the bill, explained that examination of contractors' records by the Comptroller General would enable "the General Accounting Office to look behind the * * * [price] which had been established * * * [to assess whether it was] excessive" and would act as a "safeguard against waste and extravagance" in government procurement. 97 Cong. Rec. 13198 (1951). See also *id.* at 13373 (remarks of Rep. Hoffman) ("GAO is * * * the most effective agency we have against fraud and extravagance and waste and all those things"); (*ibid.*) (remarks of Rep. Church) (legislation "is necessary in the interest of integrity or economy"). As Representative Hardy emphasized:

> The major purposes of the bill are twofold: One, to give the Comptroller General the proper tools to do the job the Congress has instructed him to do; and, two, to provide a deterrent to improprieties and wastefulness in the negotiation of contracts.

Id. at 13198; see also *id.* at 13200 (remarks of Rep. Hardy).

In enacting the access-to-records statutes, Congress "clearly understood * * * that there are a lot of other situations besides those involving fraud which might be uncovered." 97 Cong. Rec. 13199 (1951) (remarks of Rep. Hardy). Because of its concern that, "aside from any intentional liberality on the part of the Government contracting officer, there is every chance in the world that the Government will come out on the short end of the deal," Congress sought to "enable the * * * [Comptroller General] to check the transaction, both from the Government records and the contractors' books (*id.* at 13198) (remarks of Rep. Hardy). See also *id.* at 13377 (remarks of Rep. Hoffman and Rep. Hardy). And, in accordance with

the Comptroller General's responsibility to investigate and make recommendations regarding economy and efficiency in public expenditures (see page 13, *supra*), Congress fully expected that "if * * * [GAO] should find that the * * * [price was] excessive, it could, and undoubtedly would, bring the facts to the attention of the contracting officer, and possibly in an extreme case, it might call attention of the Congress to the situation" (*id.* at 13198 (remarks of Rep. Hardy)). See also H.R. Rep. No. 791, *supra*, at 5 (GAO letter stating that "any abuses discovered by the General Accounting Office in exercising the authority contained [in the bill] promptly will be brought to the attention of the proper officials, and, if warranted, to the attention of the Congress"); S. Rep. No. 603, *supra*, at 4 (same).[10]

In passing this legislation, Congress also was well aware of the broad authority it was conferring upon the Comptroller General. For example, Representative Hoffman stated that "[t]he GAO under this bill can go into the books * * * and get * * * anything and everything they want * * *" (97 Cong. Rec. 13373 (1951)). Similarly, Representative Harvey noted that a contractor "would be subject to having all of his books opened up for inspection by Government officials" (*id.* at 13372). Indeed, in introducing an amendment to exempt certain suppliers of materials, Representative Harvey objected to the expansive terms of the Hardy bill (*id.* at 13376):

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[10] Respondent concedes (Br. in Opp. 9) that the purpose of the statutes "was to empower the Comptroller General to audit governmental contracts' costs and performance to the end that the government be guarded against excessive cost or waste."

> Some little contractor or manufacturer who may be using only 10 percent of his capacity for the production of goods for the prime contractor, but because of that—and he cannot afford to keep a separate set of books for that 10 percent—it means that every section of his books will have to come under the complete scrutiny of the GAO. He is going to be harassed no end to try to break down production costs and show the details on that 10 percent of his production that went into the general program of defense. While I credit the author of the bill with the very best of intentions, I do not think he understands or fully appreciates what the ultimate effect will be upon our economy if every person who is manufacturing anything is going to have to supply all the answers to the GAO on everything that he manufactures, and such is literally going to be the impact of the bill if this amendment is not included.

Representative Hill reiterated this concern, arguing that GAO could "come out to that little town and examine all of his books because he happens to be making a few pieces of equipment for a subcontractor in New York City" (*ibid.*). Representative Hoffman also supported adoption of the amendment because "[i]f someone out in the country makes a contract for * * * an item which may be 10 percent of the total production, * * * under this bill, if it goes through [without the amendment], the GAO can send someone out there and go through the books, not only with reference to that one item of 10 percent which went into production for the government, but into all of his other business where that same item was used" (*id.* at 13377). However, Representative Hardy opposed the amendment on the ground that it "would make it impossible frequently to obtain information which would be vital in a study of a contract" (*id.*

at 13376), and the Harvey amendment was defeated (*id.* at 13377).

We recognize that Representative Hardy's bill did not originally contain the provision that records examined by GAO be "directly" pertinent to a government contract. The word "directly" was added as a floor amendment offered by Representative Hoffman, who explained that "[t]he purpose is to limit the 'snooping' that may be carried on under this bill * * *." 97 Cong. Rec. 13377 (1951). But Representative Hardy did not object to this modification, which passed without debate or discussion (*ibid.*). In these circumstances, and especially given Representative Hardy's earlier opposition to the Harvey amendment and his belief that "those with nothing to hide have nothing to fear by opening their books to the General Accounting Office" (*id.* at 13197), it is unreasonable to conclude that Representative Hoffman's amendment significantly altered the scope or intendment of the Hardy bill or was intended to bar the Comptroller General's access to records legitimately needed, as in this case, to protect against waste, excessive prices, and ineffective procurement. See *Eli Lilly & Co.* v. *Staats*, *supra*, 574 F.2d at 916 & n.8. See also Comment, *The Comptroller General's Authority to Examine the Private Business Records of Government Contractors: Eli Lilly & Co.* v. *Staats*, 92 Harv. L. Rev. 1148, 1157-1158 (1979) ("[t]he court [in *Eli Lilly*] correctly rejected Lilly's argument that the insertion of the word 'directly' into the 'directly pertinent' formula sharply narrowed the scope of inquiry to be allowed the GAO").

Prior to the decision in this case, the courts of appeals had broadly construed the access-to-records provisions to effectuate the congressional intent to enable

GAO to detect government inefficiency or wastefulness and to recommend improvements in the system of negotiated contracts. As the Ninth Circuit explained in *Hewlett-Packard Co.* v. *United States*, *supra*, the Comptroller General is empowered to investigate whether a contractor's costs are "out of line with the contract price" and hence whether "the contract may have been an inappropriate means of meeting this particular procurement need of the Government. While this appraisal could not affect these particular contracts, it could lead to the use of other methods of meeting future procurement needs" (385 F.2d at 1016).[11] Similarly, in *Eli Lilly & Co.* v. *Staats*, *supra*, the Seventh Circuit followed "the broad reading of *Hewlett-Packard* * * * [as] most consistent with the plain meaning of the statutory language and with the legislative history" (574 F.2d at 913), and concluded that Congress envisioned "an inquiry [by the Comptroller General] into whether costs are excessive" (*id.* at 915).[12]

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[11] In *Hewlett-Packard*, GAO "requested all books, documents, papers or records * * * 'relating to the pricing and cost of performance, support for prices charged to the Government, and such other necessary information which would permit * * * [GAO] to review the reasonableness of the contract prices * * *'" (385 F.2d at 1015). The district court granted the government's motion for summary judgment "and entered a judgment substantially as prayed for in the complaint" (385 F.2d at 1013-1014), declaring that GAO "could examine any such records 'relating to the cost of producing the items furnished by Hewlett-Packard Company under the aforesaid contracts, including costs of direct material, direct labor and overhead costs * * *'" (385 F.2d at 1016). The court of appeals affirmed.

[12] The Seventh Circuit's analysis of the congressional purpose underlying the access-to-records statutes is discussed with approval in Comment, *supra*, 92 Harv. L. Rev. at 1157-1158 & nn.67-68.

Commentators have likewise recognized the broad remedial purpose of the access-to-records provisions. As Professor Mosher explained:

> The GAO audits a very limited sample of contracts annually, primarily to identify and evaluate the efficiency and effectiveness of procurement policy, pricing, controls, and auditing. Its focus is not upon individual contracts or contractors but upon the effectiveness of the systems and criteria whereby contracts are negotiated, carried out, and audited by the executive agencies. Its aims are primarily to develop and make recommendations for improvements in the process, not to seek out individual culprits.

See F. Mosher, *The GAO: The Quest for Accountability in American Government* 318 (1979). See also, *e.g.*, G. Cuneo, *Government Contracts Handbook* 183 (3d printing 1964) ("GAO audits are basically a post-performance audit review, and are related to the responsibilities of the Comptroller General to keep Congress informed of the degree of efficiency with which the executive agencies perform their procurement functions involving the administration of appropriated funds"); I R. Nash & J. Cibinic, *supra*, at 381 ("[i]n negotiated contracts, Congress has been continually concerned with the possibility that unreasonable prices will be paid"); Cibinic & Lasken, *supra*, 38 Geo. Wash. L. Rev. at 388 ("[n]ot to be overlooked is Congress' deep and abiding distrust of the negotiation process"). Furthermore, "[s]uch reports [by GAO to Congress based on the access-to-records provisions] can be very useful. They can and have sharpened the Government's negotiation practices." *Id.* at 389. See also J.A. 100.

As this Court has observed, the "objective * * * [in construing a statute] is to ascertain the congressional

intent and give effect to the legislative will." *Philbrook* v. *Glodgett*, 421 U.S. 707, 713 (1975). See also, *e.g.*, *United States* v. *American Trucking Associations*, 310 U.S. 534, 542 (1940) ("[i]n the interpretation of statutes, the function of the courts is * * * to give effect to the intent of Congress"). And, of course, a court's "individual appraisal of the wisdom or unwisdom of a particular course consciously selected by the Congress is to be put aside in the process of interpreting a statute. Once the meaning of an enactment is discerned * * * the judicial process comes to an end." *Rubin* v. *United States*, No. 79-1013 (Jan. 21, 1981), slip op. 7 n.8, quoting *TVA* v. *Hill*, 437 U.S. 153, 194 (1978). See also, *e.g.*, *Commissioner* v. *Bilder*, 369 U.S. 499, 504 n.5 (1962) ("the equitable considerations which the respondent brings to bear in support of her construction * * * are of course beside the point in this Court, since we must give the statute effect in accordance with the purpose so clearly manifested by Congress"). In ignoring the legislative history of the access-to-records statutes and rejecting the uniform understanding of those provisions by courts and commentators, the Second Circuit's decision impedes GAO's statutory responsibilities and defeats the intention of Congress.

C. GAO's Interpretation Of The Access-To-Records Provisions Is A Consistent And Longstanding Construction That Congress Has Recognized And Never Disapproved

From the time of their enactment in 1951, the access-to-records statutes consistently have been construed by GAO to authorize the examination of all cost records relating to the reasonableness of the contract price, and Congress, although aware of this construction, has not disapproved the agency's inter-

pretation or amended the statutes to reject that position. See J.A. 99.

Shortly after passage of the access-to-records provisions, the Comptroller General stated in a public decision that the statutes "were intended, among other things, to afford a means whereby the Congress could be informed of any excessive or unreasonable payments to contractors holding negotiated contracts * * *." 32 Comp. Gen. 277, 278 (1952). More than a decade later, the Comptroller General expressed the same view that "the overall objective [of an audit] is to review the manner in which the contracted activities of Federal agencies are administered and to recommend, where appropriate, corrective or improvement actions deemed necessary or desirable to promote greater efficiency or economy in Federal expenditures. * * * The audit reports of the General Accounting Office are intended * * * to inform the Congress and/or the Federal agencies concerned on the results of audit work on procurement contracts * * * and to make recommendations, based on such work, leading to greater efficiency and economy in such expenditures." United States General Accounting Office, *Audits of Government Contracts* 8-9, 16 (1966); see also *id.* at 19-20.

GAO's construction of the access-to-records statutes also has been repeatedly presented to Congress, which has never indicated its disapproval of the agency's view. For example, in the 1956 Annual Report to Congress under 31 U.S.C. 53(a), the Comptroller General explained that GAO "audits are designed to evaluate the manner in which agency representatives perform their respective functions relating to negotiated contracts, and include a review of the contractor's organization, procedures, and business methods for the purpose of evaluating the protection which

has been afforded the Government's interests." *Annual Report of the Comptroller General of the United States for the Fiscal Year Ending June 30, 1956*, at 23 (1956). See also G. Cuneo, *supra*, 184 & n.10.

In 1963, Robert Keller, General Counsel of GAO, appeared before a congressional subcommittee that was "concerned with the availability of cost data in negotiated contracts" and "the need for, or desirability of, recommending legislative action" in light of Hewlett-Packard's recent refusal to permit inspection of its cost records pursuant to the access-to-records provisions. See *Hearings on Relation of Cost Data to Military Procurement Before the Subcomm. for Special Investigations of the House Comm. on Armed Services*, 88th Cong., 1st Sess. 2, 3 (1963). Focusing on "the relationship of cost data to procurement and to post-audit review * * * [and on GAO's function] to make recommendations looking to greater economy and efficiency in public expenditures" (*id.* at 5), Mr. Keller testified that "[o]ur experience indicates the need for careful examination into the reasonableness of accepting catalog or other established prices for negotiated procurements, particularly where contractors have resisted requests by the procurement agencies for cost data to support price proposals and quotations" (*id.* at 8).[13] Emphasizing the impor-

[13] See also *Eli Lilly & Co.* v. *Staats*, *supra*, 574 F.2d at 915 ("[the] argument that Congress could not have intended to inquire into wastefulness in contracts such as the one here in which the drugs were supplied to the Government 'at a fixed price at or below the wholesale market price' * * * ignores the fact that the information sought by the Government may show that the prices it paid were nevertheless much too high"); *Hearings on Relation of Cost Data to Military Procurement*, *supra*, at 6-8 (statement of GAO General Counsel Keller) (citation omitted).

tance of "obtain[ing] reasonable assurance that the prices [the Government] contracted to pay were fair to the Government as well as to the supplier" (*id.* at 12) and of "evaluating the reasonableness of the prices quoted" (*id.* at 15), Mr. Keller explained GAO's construction of the access-to-records provisions (*id.* at 6, 10-11, 15; emphasis added):

> With the increased use of negotiated contracts for the purchase of supplies and equipment, the Congress, in order to assure that such supplies and equipment are obtained at reasonable prices, has provided that negotiated contracts shall include a clause giving the Comptroller General * * * the right to examine any pertinent books and records of the contractor * * * involving transactions related to * * * work under the contract.
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> * * * * *
>
> It is our position that the contract clause and the statute give us the right to examine the cost records of the contractor and other pertinent data that relates to the items included in the contract, *in sufficient completeness and detail to permit us to determine the reasonableness of the negotiated prices.*
>
> We believe our position is supported by the language of 10 U.S.C. 2313(b) and the contract provision and, to an even greater extent, by the legislative history of the statute * * *.
>
> We believe, further, that our position is supported by the fact that our interpretation of the statute has been consistently applied since its enactment without objection by the Congress and, therefore, should be given the consideration normally accorded longstanding administrative interpretations of statutes.
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> * * * * *

> [I]f Hewlett-Packard is successful in preventing the General Accounting Office from obtaining access to its records relating to such negotiated contracts, the Government will be deprived of the most important means for examining into the reasonableness of contract prices.

And, with particular pertinence to the present case, Mr. Keller stated that GAO could "go beyond direct manufacturing costs" into such areas as "how research costs are allocated as between the Government contract and commercial business" (*id.* at 23). Representative Hardy, based on his "background of personal knowledge * * * [of] what congressional intent was at the time * * * [the statutes were] originally passed" (*id.* at 3), commented that Mr. Keller had "stated this case very well as to the necessity for having a contract provision permitting audits of negotiated contracts" (*id.* at 23).

Two years later, GAO again apprised Congress of its construction of the access-to-records provisions. Comptroller General Campbell testified that these provisions "permit detailed examination of a contractor's records to insure the necessary degree of supervision and control. In other words, the clear intent of the statute is to provide for the examination by the General Accounting Office of such records of a contractor, to such an extent as will permit a meaningful examination of the reasonableness of the prices charged to the Government." *Hearings on Comptroller General Reports to Congress on Audits of Defense Contracts Before the Subcomm. on Military Operations of the House Comm. on Government Operations*, 89th Cong., 1st Sess. 44 (1965). Mr. Campbell later reiterated GAO's position "that the contract clause and the statute on which the clause is based gives us the right to examine the cost records of the

contractor and other pertinent data that relate to the items included in the contract, in sufficient completeness and detail to permit us to examine into the reasonableness of the negotiated prices. * * * The fact that, in [the] final analysis, we may not be able to question the legality of particular contract transactions does not preclude our reporting to the Congress and to the responsible administrative agencies that such transactions are wasteful or extravagant or that a particular contract transaction illustrates the need for an improvement in existing procurement or management procedures" (*id.* at 45, 48).[14] And General Counsel Keller also stated the agency's view "that the Congress intended the General Accounting Office to examine the books and records of the contractor to make certain that the Government was getting a fair deal out of negotiated contracts" (*id.* at 147). See also *ibid.* (statement of Comptroller General Campbell) (if the contractor "had his records commingled * * * [GAO] would have to see everything," including records not otherwise covered by the access-to-records provisions).

In 1971, Congress was again advised of GAO's interpretation of the access-to-records provisions. Paul Shnitzer, Assistant General Counsel of GAO, testified that such access "is very good for the purpose of determining what costs the contractor actu-

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[14] Comptroller General Campbell's statement was clearly understood by Mr. Charles I. Derr, Senior Vice President, Machinery & Allied Products Institute, who described GAO's position to be "that the statute should be construed as broadly as is necessary in order to permit [GAO] to determine whether contract prices are reasonable." *Hearings on Comptroller General Audits, supra,* at 513; see also *id.* at 503 (statement of William J. Healey, staff counsel to the Machinery & Allied Products Institute).

ally incurred in the performance of the contract as compared to the contract price." *Hearings on Competitive Problems in the Drug Industry Before the Subcomm. on Monopoly of the Senate Select Comm. on Small Business*, 92d Cong., 1st Sess. 8018 (1971). Mr. Shnitzer then elaborated (*id.* at 8018-8019):

> What I am saying is, and we do have a case which ultimately went up as far as the Supreme Court, is that under our 1951 authority, the contract is required to include a provision which gives the GAO the right to examine records of costs, direct and indirect, generated in the performance of that contract. So if a contract is awarded to company A and it comes within the purview of this—it is a negotiated contract for, let us assume, $100,000—we would have a right then to go back and examine the records of company A—the cost records, direct and indirect, to determine how much it cost him to perform that contract * * *.

In light of this history, the court of appeals was plainly unwarranted in rejecting GAO's interpretation of the access-to-records provisions. See *Eli Lilly & Co.* v. *Staats*, *supra*, 574 F.2d at 915. The court failed to heed the " 'venerable principle that the construction of a statute by those charged with its execution should be followed unless there are compelling indications that it is wrong * * *.' " *E. I. du Pont de Nemours & Co.* v. *Collins*, 432 U.S. 46, 54-55 (1977), quoting *Red Lion Broadcasting Co.* v. *FCC*, 395 U.S. 367, 381 (1969). " 'To sustain * * * [GAO's] application of this statutory term, we need not find that its construction is the only reasonable one, or even that it is the result we would have reached had the question arisen in the first instance in judicial proceedings.' " *Udall* v. *Tallman*, 380 U.S.

1, 16 (1965), quoting *Unemployment Comm'n* v. *Aragon*, 329 U.S. 143, 153 (1946). Rather, "[i]t is settled that courts should give great weight to any reasonable construction of a regulatory statute adopted by the agency charged with the enforcement of that statute." *Investment Company Institute* v. *Camp*, 401 U.S. 617, 626-627 (1971). And this principle is particularly apt where, as in this case, there is a "longstanding and consistent administrative interpretation" (*Zenith Radio Corp.* v. *United States*, 437 U.S. 443, 450 (1978)) that " 'involves a contemporaneous construction of [the] statute by the [persons] charged with the responsibility of setting its machinery in motion' " (*Andrus* v. *Shell Oil Co.*, No. 78-1815 (June 2, 1980), slip op. 10, quoting *Norwegian Nitrogen Co.* v. *United States*, 288 U.S. 294, 315 (1933)).

Moreover, judicial deference to the agency's interpretation of a statute is especially appropriate " 'when Congress has refused to alter the administrative construction' * * * [and] that construction accords with well-established congressional goals." *Board of Governors of the Federal Reserve System* v. *First Lincolnwood Corp.*, 439 U.S. 234, 248, 251 (1978), quoting *Red Lion Broadcasting Co.* v. *FCC*, *supra*, 395 U.S. at 381. "[O]nce an agency's statutory construction has been 'fully brought to the attention of the public and the Congress,' and the latter has not sought to alter that interpretation * * *, then presumably the legislative intent has been correctly discerned." *United States* v. *Rutherford*, 442 U.S. 544, 554 n.10 (1979), quoting *Apex Hosiery Co.* v. *Leader*, 310 U.S. 469, 489 (1940). Here, "[i]n the * * * years during which [GAO] has consistently * * * [adhered to its position], Congress has never expressed its disapproval, and its silence in this regard

suggests its consent to [GAO's] practice." *EEOC* v. *Associated Dry Goods Corp.*, No. 79-1068 (Jan. 26, 1981), slip op. 9-10 n.17.

In these circumstances, GAO's interpretation of the access-to-records statutes should be followed.

D. The Access-To-Records Provisions Authorize The Comptroller General To Examine Respondent's Records Pertaining To Its Costs Of Research And Development, Advertising And Promotion, Distribution, And Administration

In light of the legislative history and administrative interpretation of 10 U.S.C. 2313(b) and 41 U.S.C. 254(c), the access-to-records provisions should be construed to authorize the Comptroller General to examine all of a contractor's cost records that are necessary and appropriate to determine whether the price charged the government was "extravagan[t]" "excessive," or "wasteful[]." 97 Cong. Rec. 13198 (1951) (remarks of Rep. Hardy). Any lesser right of access would seriously impair the Comptroller General's statutory responsibility to determine the reasonableness of the contract price and the adequacy of the protection afforded the government in negotiated procurements. Applying this standard to the present case, it is clear that the Comptroller General is entitled to access to respondent's cost records pertaining to research and development, advertising and promotion, distribution, and administration.

As the Seventh Circuit recognized in *Eli Lilly & Co.* v. *Staats*, *supra*, "it is hard to imagine anything more directly related to a contract than the cost of producing the items covered by it or the matters going into the makeup of the price" (574 F.2d at 913). See also *Hewlett-Packard Co.* v. *United States*, *supra*, 385 F.2d at 1016. The court of appeals in

Eli Lilly found that the records requested by GAO came well within the terms of the access-to-records provisions (574 F.2d at 914; footnote omitted):

> In response to plaintiff's argument that including these items would not give full effect to the limits on disclosure implied by the use of the word "directly," without disputing that "directness" is a difficult concept to define, it should be noted that costs such as research and development at the least appear to have a logical, causal and consequential relationship to a portion of the price of the products purchased by the Government. Further, contrary to plaintiff's contention, such costs are not "remote" within the established definitions of that term in relation to at least a portion of the price because their inclusion in the price of the product is not unforeseeable once the costs are incurred, nor is their impact on a part of the price significantly altered by any intervening cause.

This analysis accords with the purpose of the access-to-records statutes to determine whether the government "c[a]me out on the short end of the deal" (97 Cong. Rec. 13198 (1951) (remarks of Rep. Hardy)) and with GAO's construction of the access provisions to allow an "examin[ation of] the cost records of the contractor * * * in sufficient completeness and detail to permit us to examine into the reasonableness of the negotiated prices" (*Hearings on Comptroller General Audits*, *supra*, at 45 (statement of Comptroller General Campbell)).[15]

Indeed, the records sought in this case are particularly important in the context of pharmaceutical contracts. The manufacturing and distribution costs

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[15] See also Comment, *supra*, 92 Harv. L. Rev. at 1157-1158 & nn.67-68.

of individual pharmaceutical products have been estimated to constitute as little as 9% of the sale price of such products. See *Eli Lilly & Co.* v. *Staats, supra,* 574 F.2d at 913, citing Rucker, *Public Policy Considerations and the Pricing of Prescription Drugs in the United States,* 4 Int'l J. Health Services 171, 173 (1974).[16] See also *SmithKline Corp.* v. *Staats, supra,* 483 F. Supp. at 722. At the same time, "the drug industry devotes a 'significant portion' of its sales revenues (11.9 percent of the industry's 1971 sales) to research of new and improved ethical drugs and biological products" (J.A. 96). See also Reekie, *Price and Quality Competition in the United States Drug Industry,* 26 J. Indus. Econ. 223, 235 (1978) ("innovative outlays [are] by far the largest forms of outlay in the drug industry; manufacturing and other short-run variable costs form only a small proportion of total costs"). To confine access by the Comptroller General to records of the relatively minor direct costs (such as manufacture and delivery), and to exclude records of virtually all other costs (such as research and development) that are more substantial than the direct costs, would plainly frustrate GAO's responsibility to examine the contractor's cost

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[16] Mr. Rucker states (*ibid.*):

> The first major issue deals with the proportion of product price that is accounted for by direct manufacturing and distribution costs. Table 1, which presents data for nine important branded products marketed in the U.S.[,] shows a median of 91 per cent as the proportion of supplier's revenue consumed by indirect factors, such as research and development, promotion, general administrative expense, taxes, and profit. Thus we see that only a very small percentage of wholesale price represents the direct expense of making the pharmaceutical agent available for patient consumption.

records in order to assess the fairness of the contract price.

Nevertheless, the court below concluded that such a limitation was required in this case because the records in question involve costs that respondent neither allocates to particular products or contracts nor calculates on a product basis in setting prices.[17] This analysis, which fails even to mention GAO's legitimate need for access to the requested records, is misconceived. First, the government cannot be bound by the accounting method respondent has established for its own purposes. Cf. *Exxon Corp.* v. *Department of Revenue of Wisconsin*, No. 79-509 (June 10, 1980), slip op. 12-14. If respondent had fully allocated its costs, GAO's right to conduct an inspection adequate to evaluate the reasonableness of the contract price would be clear. No different outcome is warranted simply because respondent has chosen to allocate only some of its costs to particular contracts or products. Indeed, the logical consequence of the court of appeals' decision is that respondent would not be obliged to open any of its books to the Comptroller General if, for internal bookkeeping purposes, it chose to allocate none of its costs to a particular contract or product.[18]

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[17] It does appear, however, that respondent, by setting its prices in part on the basis of its historical pricing and that of its competitors, takes into account its unallocated costs (J.A. 120, 133, 137-138).

[18] The courts below purported (Pet. App. 12a) to "agree with the government that the issue [of access] should not depend entirely on a contractor's bookkeeping method, *i.e.*, whether it does or does not assign particular costs to particular contracts or products." In the end, however, GAO was not afforded access to any records of costs that respondent does not in fact assign. See J.A. 120-129.

Moreover, respondent's election to keep its business records on the basis of unallocated costs cannot obscure the fact that an examination of these costs is necessary for the Comptroller General to discharge his statutory responsibility to determine whether the government has been charged a reasonable price. To operate profitably, respondent must recover its costs from sales revenues, and it uses the payments by the government under the contracts at issue, as part of commingled general revenues, to help defray its unallocated expenses (J.A. 96, 103, 106, 137-140).[19] Accordingly, respondent's costs, even though unallocated, are critical to an assessment of the fairness of the contract price and the advisability of continued adherence by the government to the negotiated procurement methods employed here. If respondent's total costs are substantially lower than the prices paid by the government, the Comptroller General may recommend that the Department of Defense and the Veterans Administration adopt different procurement practices in the future. See *Hewlett-Packard Co.* v. *United States*, *supra*, 385 F.2d at 1016 ("[w]hile this appraisal could not affect these particular contracts, it could lead to use of other methods of meeting future procurement needs").

Nothing in the language of the statutes or their legislative history justifies the restriction imposed by the court of appeals on the applicability of the access provisions to respondent's unallocated costs. On the contrary, the court's construction would effectively defeat the congressional objective to guard against waste, extravagance, and excessive pricing. And, as explained in *Eli Lilly & Co.* v. *Staats*, *supra*, "[t]he mere fact that, as [respondent] asserts, it does not

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[19] The government was charged respondent's normal wholesale price (J.A. 133, 136).

or even could not allocate costs such as research and development to an individual contract does not undercut the proposition that those costs are directly pertinent to an individual contract but merely indicates that they are directly pertinent to more than one individual contract" (574 F.2d at 914). Especially in light of the cost structure in the pharmaceutical industry (see pages 31-32, *supra*), it is manifest that the Comptroller General's inquiry into the appropriateness of the contract price cannot be limited to allocated costs of production and delivery and must include such significant unallocated costs as research and development, advertising and promotion, distribution, and administration. Respondent's contrary position would plainly thwart the congressional policy and would reduce the Comptroller General's exercise of his remedial authority to an empty and ineffectual endeavor.[20]

The question of cost allocation is a familiar one in the area of government contracts. For example, 41 C.F.R. 1-3.1220(b)(4), which is applicable to negotiated procurements (see 41 C.F.R. 1-3.000, 1-3.100), defines "allocate" to "include[] both direct assign-

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[20] Of course, insofar as respondent has allocated a given category of costs, the Comptroller General would be entitled to examine records relating only to such costs as have been attributed to the product supplied the government (together with records necessary to verify such data). To the extent that broader access is required in this case, it is the result of respondent's decision not to allocate its costs and the consequent need for the Comptroller General to construct a measure of those costs in order to determine the reasonableness of the contract price. Whatever the nature of a contractor's accounting system, the Comptroller General's authority remains the same—to examine those costs necessary to determine whether the contract price was "extravagan[t]," "excessive," or "wasteful[]." 97 Cong. Rec. 13198 (1951) (remarks of Rep. Hardy).

ment of cost and the reassignment of a share from an indirect cost pool." See also 41 C.F.R. 1-3.1220(b)(14) and (15), 1-15.202, 1-15.203 (definitions of "indirect cost" and "indirect cost pool"). In addition, 41 C.F.R. 1-15.201-4 provides that

> a cost is allocable to a Government contract if it:
>
> (a) Is incurred specifically for the contract;
>
> (b) Benefits both the contract and other work, or both Government work and other work, and can be distributed to them in reasonable proportion to the benefits received; or
>
> (c) Is necessary to the overall operation of the business, although a direct relationship to any particular cost objective cannot be shown.

And, with particular reference to research and development, 41 C.F.R. 1-15.205-35 sets forth the applicable principles to calculate the portion of such costs attributable to a government contract. If the contracts in this case were cost-based rather than fixed-price, respondent would be entitled to claim reimbursement for its indirect costs that were allocable to those contracts. There is no reason to conclude that the same approach is inapplicable where, as here, it is GAO that seeks to make the allocation in order to review the adequacy of the protection afforded the government's interest in negotiated procurement.[21]

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[21] We note that in those access-to-records cases in which the government has prevailed, there was apparently no difficulty in fashioning suitable relief. (For the convenience of the Court, we have appended a copy of the unpublished order of the district court on remand in *Eli Lilly & Co.* v. *Staats*, *supra*. See Appendix, *infra*, 1a-5a.) Courts have solved similar problems, involving inspection of records showing a company's profit or loss on particular product lines, in the context of

Finally, the court of appeals incorrectly relied on the presumed intentions of the parties to hold that the contractual access-to-records clause does not encompass the materials sought by the Comptroller General concerning respondent's unallocated costs. In view of the decision in *Hewlett-Packard*, GAO's public statements of its construction of the access provisions (see pages 23-28, *supra*), and the general recognition of GAO's position (see page 21, *supra*), respondent was on notice of GAO's interpretation and cannot be assumed to have had a contrary understanding. See *Eli Lilly & Co.* v. *Staats*, *supra*, 574 F.2d at 918.[22] But, more important, the meaning of the contractual access-to-records clause does not rest on the understanding of the parties. The clause was statutorily required to be included in the contract, and its content is necessarily determined by those statutes rather than by the parties' intentions. See, *e.g.*, *Federal Crop Insurance Corp.* v. *Merrill*, 332 U.S. 380, 383-385 (1947); *De Matteo Const. Co.* v. *United States*, 600 F.2d 1384, 1391 (Ct. Cl. 1979); *Jackson* v. *United States*, 573 F.2d 1189, 1194 (Ct. Cl. 1978); *G. L. Christian and Associates* v. *United States*, 320 F.2d 345, 351 (Ct. Cl.), cert. denied, 375 U.S. 954 (1963); cf. *United States* v. *Wunderlich*, 342 U.S. 98, 100 (1951).

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discovery under the Federal Rules of Civil Procedure. See, *e.g.*, *United States* v. *International Business Machines Corp.*, 66 F.R.D. 186 (S.D.N.Y. 1974).

[22] See also, *e.g.*, *Stencel Aero Engineering Corp.* v. *United States*, 431 U.S. 666, 674 n.8 (1977); *Bowers Dredging Co.* v. *United States*, 211 U.S. 176, 188 (1908); *Jamesbury Corp.* v. *Worcester Valve Co.*, 443 F.2d 205, 210 n.7 (1st Cir. 1971); *Perry and Wallis, Inc.* v. *United States*, 427 F.2d 722, 725 (Ct. Cl. 1970); I *Chitty on Contracts* ¶ 613, at 288 (23d ed. 1968); 3 A. Corbin, *Contracts* § 537, at 45, § 556, at 243 (1960).

CONCLUSION

The judgment of the court of appeals should be reversed.

Respectfully submitted.

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FEBRUARY 1981

APPENDIX

UNITED STATES DISTRICT COURT
SOUTHERN DISTRICT OF INDIANA
INDIANAPOLIS DIVISION

No. IP 75-72-C

ELI LILLY AND COMPANY

v.

ELMER B. STAATS,

COMPTROLLER GENERAL OF THE UNITED STATES,
DEFENDANT,

UNITED STATES OF AMERICA, INTERVENOR

JUDGMENT

This matter comes to the Court upon remand from the U.S. Court of Appeals for the Seventh Circuit for proceedings consistent with its opinion herein. In accordance with the Mandate of the U.S. Court of Appeals for the Seventh Circuit this Court does now vacate its judgment of November 30, 1976. The parties, to avoid further litigation and to resolve their differences, agree and consent to the terms of this judgment. Therefore, the Court, being duly advised in the premises, ORDERS this 28th day of November 1978, that:

1. The Motion for Summary Judgment filed on behalf of the United States of America, defendant-intervenor, on its counterclaim against the plaintiff, Lilly, be and the same hereby is, granted as reflected in this order, and Lilly's Cross Motion is denied.

2. The Comptroller General of the United States and his duly authorized representatives have the right to examine all books, documents, papers, or records directly relating to the pricing and cost of producing items furnished by plaintiff, Lilly, under the following contracts numbered: V797P-5169(C), DSA120-74-C-1401, DSA120-74-C-0125, DSA120-74-C-1639, DSA120-74-C-0896, DSA120-74-C-1176 and DSA120-74-C-1640, including, but not limited to, records of experienced costs, including costs of direct materials, labor, overhead, and other corporate costs, records in support of prices charged to the Government and such other necessary information which would permit representatives of the Comptroller General of the United States to review the reasonableness of the contract prices provided for in the aforesaid contracts, except that no access is granted to any additional documents, and no information need be produced relating to classes of costs that have no more than a *de minimis* impact on the price of a product purchased by the Government.

3. The plaintiff, Lilly, its officers, agents, servants, attorneys, employees and all persons in active concert or participation with them who receive actual notice of an order by personal service or otherwise, are enjoined from preventing the duly authorized representatives of the Comptroller General of the United States from exercising the right to examine granted hereby and plaintiff Lilly, including its officers and subordinates, are directed to have available on the premises of Lilly, Indianapolis, Indiana, and its other principal offices wherever located, such books and records at a time and date to be fixed by the Court upon application of the Comptroller General of the United States or his duly authorized representatives.

4. The original and all copies of every book, report, paper, record, and other document (all hereinafter referred to as "document"), designated as confidential by Lilly or any of its divisions or subsidiaries and provided or otherwise made available to the Comptroller General or any of his successors, agents, employees, or subordinates (all hereinafter referred to as "the Comptroller General"), and every summary thereof and extract therefrom, and all data and information contained therein, including accountants' workpapers (all hereinafter referred to as "data"), shall be held in confidence and shall not be provided or otherwise made available by the Comptroller General to any other person or agency except as provided in subparagraphs (a) and (b) below. No copies of Lilly's documents shall be included in accountants' workpapers without the approval of Lilly.

5. Any document and data referred to in the above paragraph shall be used by the Comptroller General solely for the purpose of a contract study and no information other than that pertaining to Lilly's government business shall appear in any report by the Comptroller General or otherwise be made public. Upon completion of that study, the Comptroller General shall immediately return to Lilly the originals and all copies of all documents described in that paragraph. Any data in which Lilly, any of its divisions or subsidiaries, or any product manufactured or sold by any of them are or may be directly or indirectly identified which the Comptroller General deems it necessary to retain shall be deposited with and maintained by the Comptroller General under security measures to be agreed upon by the parties. Any such data which the Comptroller General does not deem it necessary to retain shall be destroyed immediately upon the completion of the study. Access to such data

by any person shall be permitted only upon written authorization of the Comptroller General and only when permitted under the subparagraphs following next denominated (a) and (b).

(a) Any of the data referred to in the above paragraphs may be published, provided to, or otherwise made available to a person or agency other than the Comptroller General if the data are published, provided, or made available in such a way that any direct or indirect identification of Lilly, any of its divisions or subsidiaries, or any product manufactured or sold by any of them, is not reasonably possible. Lilly shall be afforded a reasonable opportunity to examine and offer its comments regarding any data considered for release, including any report issued by the Comptroller General that includes such data, before release of the data or report.

(b) The Comptroller General may comply without regard to the limitations of this Order set forth in subparagraph (a) above, with an official written request for any of the data referred to above submitted to him by either House of Congress, or any committee of the House of Representatives or the Senate, or any joint committee of the two Houses, having jurisdiction over the subject matter of said study, to the extent authorized and directed by law. The Comptroller General will cause prompt notice of any such request to be given to Lilly and to this Court at least seven calendar days prior to furnishing the data requested.

6. The Comptroller General and the United States shall notify Lilly promptly of any request for disclosure, subpoena *duces tecum*, civil action, or other

order or application for an order seeking production, release, or disclosure of any documents or data referred to above, and further agree to use their best efforts to protect the confidentiality of such documents or data, except as provided in subparagraph (a) above, including resort to appropriate judicial remedies and cooperation with Lilly in such efforts.

7. The Court shall retain jurisdiction to interpret and enforce the terms of this Consent Judgment, upon application of any party.

8. The costs of this action shall be taxed against plaintiff, Lilly.

CALE J. HOLDER
United States District Judge

Done at Evansville, Ind.
this 28 day of Nov., 1978.

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IN THE

Supreme Court of the United States

OCTOBER TERM, 1980

No. 80-264

ELMER B. STAATS, COMPTROLLER GENERAL OF THE UNITED STATES, and UNITED STATES OF AMERICA,

Petitioners,

v.

BRISTOL LABORATORIES DIVISION OF BRISTOL-MYERS COMPANY,

Respondent.

ON WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE SECOND CIRCUIT

BRIEF FOR RESPONDENT

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IN THE

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BRISTOL LABORATORIES DIVISION OF BRISTOL-MYERS COMPANY,

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ON WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE SECOND CIRCUIT

Questions Presented

Under provisions in contracts between respondent ("Bristol")* and 1) the Defense Supply Agency of the Department of Defense, 2) the Veterans Administration (both agencies of the United States of America) reading in part respectively 1) "the Comptroller General and his representatives are entitled . . . to examine any books, documents, papers or records of [Bristol] that directly pertain to, and involve transactions relating to, the contract", and 2) "the Comptroller General . . . shall . . . have access to and the right to examine any directly pertinent books, documents, papers and records of [Bristol] . . . involving transactions relating to such contracts", and which provisions were authored and

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* Bristol has no parent company and no affiliate.

required by the United States government,† must Bristol be deemed to have understood that it was giving the Comptroller General access to its records of costs which had not been factored into and had played no role in determining the prices in those contracts? Absent such an understanding, must Bristol grant the Comptroller General such access?

† 10 U.S.C. 2313(b) and 41 U.S.C. 254(c).

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Respondent.

ON WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE SECOND CIRCUIT

BRIEF FOR RESPONDENT

Statement

Although, as page 5 of the government's brief ("G.B.") states, Bristol originally rejected the Comptroller General's demand for access to "records relating to the methodology and decisions involved in the firm's establishment of prices . . . (J.A. 69)", Bristol changed that position and agreed to provide these records during this case.[1]

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[1] In its memorandum in support of its first motion for summary judgment (dated July 22, 1975), Bristol stated in a footnote to page 5, "[it] does not dispute defendant's right to access to and examination of those documents identified in answers . . . 2(c) . . . to plaintiff's first set of interrogatories." Answer 2(c) had identified the "methodology and decisions" documents. J.A. 17.

Summary of Argument

It is manifest in the legislative history of 10 U.S.C. 2313 (b) and 41 U.S.C. 254(c)[2] that congress intended to be more miserly than generous in the authority contemplated thereunder for the Comptroller General.

That history does not explicate why congress adopted so unusual an approach as to require that the authority be created by contracts between sellers and federal agencies rather than simply doing so by legislative fiat. But, given that basic contract principles differ from those for construing statutory grants of administrative agency power, it must be inferred that congress meant to invoke rules that characteristically govern contracts; and they are consonant with a more restrictive than expansive legislative intent regarding the Comptroller General's access-to-records rights.

Under black letter law of contracts, the words "directly pertain to", "directly pertinent" and "involve [or "involving"] transactions relating [or "related"] to" must be given the meaning they have to reasonable business men in their ordinary usage. So construed and applied, they would not define records of costs that do not *directly* (indeed, not at all) enter into ("pertain to") determining the contracts' prices, and that are not directly involved in them, or directly related thereto.

Even under principles of statutory construction, documents and records that have nothing to do with setting the contract prices cannot be embraced as "directly" pertinent to, or involved in or related to, such contracts or to transactions relating to them.

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[2] Quoted at G.B. 1-2. Sometimes referred to hereinafter as the "Hardy amendment(s)".

ARGUMENT

I.

Legislative history clearly manifests a parsimonious intent by congress with respect to access to records by the Comptroller General.

The first statutory appearance of a clause such as those involved here was in an amendment[3] to the First War Powers Act of 1941.[3a] The primary purpose of that amendment was to enable renegotiation of contracts for the supply of commodities to the armed forces.[4] A Hardy amendment was added to the bill (S. 4266) on January 2, 1951 (96 Cong. Rec. 17122-23). It did not contain the word "directly" to modify "pertinent". Ibid.

At the next congressional session, Congressman Hardy, explaining he had not earlier realized that other laws besides the First War Powers Act of 1941 were appropriate beneficiaries for his amendment (97 Cong. Rec. 13198, col. 1, October 15, 1951), proposed similar amendments to the Federal Property and Administrative Services Act of 1949 (41 U.S.C. 454(c)) and the Armed Services Procurement Act of 1947 (10 U.S.C. 2313(b)), the sections now before this Court. 97 Cong. Rec. 1246 (February 12, 1951).

It was during the October 15, 1951 debate in the House that two clear manifestations appeared of congressional disinclination to be liberal with access-to-records privileges for the Comptroller General. The first is at the end of 97 Cong. Rec. 13198. It serves notice that congress advisedly differentiated between statutory power and contractual permission.

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[3] Pub.L. No. 81-921, ch. 1230, 64 Stat. 1257 (January 12, 1951).

[3a] 50 U.S.C. App. § 611, 55 Stat. 838, *repealed*, Pub.L. 89-544, § 8(a), 80 Stat. 651, (September 6, 1966).

[4] 96 Cong. Rec. 17042 et seq. (January 1, 1951) and 96 Cong. Rec. 17122 et seq. (January 2, 1951).

> MR. EBERHARTER. * * * * Now, I would like to ask one question: Does this refer to contracts that have been made in the past?
>
> MR. HARDY. It could not refer to contracts that have been made in the past, because it requires the insertion of a clause in contracts.
>
> MR. EBERHARTER. I see. I notice that you give power to the Comptroller General.
>
> MR. HARDY. It does not give him power to inspect the books and records, but requires that a clause be inserted in the contracts permitting him to inspect.[5]

Congressman Hardy reiterated this distinction in the subsequent session, emphasizing that the Comptroller General's right of access "is given him in the contract. The right is not given him in the bill." Idem at 13376.

There are three possible explanations of why congress adopted the unusual approach of having the Comptroller General's right-to-access be created by contractual permission rather than by statutory fiat. It either considered that doing so would give him a) broader rights, or b) narrower rights or c) make no difference at all. It could hardly have been the first. To infer the last would charge congress with a meaningless differentiation. The second—especially in context with other harmonious clues—seems the most likely.

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[5] Significantly, at one point in the House debate on Congressman Hardy's earlier amendment to the First War Powers Act of 1941, he had been questioned as to why his amendment did not give more power to the Comptroller General than simply to inspect books and records. He answered, "We are reenacting what was weak in this respect, and my purpose is to try and strengthen it so that we will at least get our foot in the door, and the Congress will have an opportunity to observe intimately just what takes place in these renegotiations. I would like to see the amendment provide greater control, but I have been unable to work out stronger wording without burdening the bill in such a way that it would be unworkable by the Departments." 96 Cong. Rec. 17045 (January 1, 1951).

At 97 Cong. Rec. 13377 (October 17, 1951), Congressman Hoffman (Michigan) proposed that the Hardy amendment be amended by inserting the word "directly" immediately before the word "pertinent". His intent was clear from his contextual comments.[6] Mr. Hardy stated, "I have no objection to the [Hoffman] amendment"; and his own, with Mr. Hoffman's added, was adopted. Ibid.

II.

The only books and records Bristol withholds from the Comptroller General are those concerning costs that did not enter into or affect determination of the prices in Bristol's contracts at issue in this case.

Since Bristol has agreed to make available to the government records relating to its production costs for the items covered by the contracts in issue, Bristol, unlike the *amici*, did not raise the broader question whether *any* cost records can be deemed directly pertinent to contracts which were not negotiated on the basis of the contractor's costs. Rather,

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[6] "Down into his place of business—and there has never been any trouble there and there is not now—come the investigators for the Labor Department, the War Labor Board fellows, and then, how they go into it, I do not know, but a fellow from the internal revenue agency and one from the Food and Drug Agency, now think of it, on one item of business that went through that plant and are the Government's men impudent, arrogant, and arbitrary? Ask the owner. Now they just take the company's time, and when you multiply that by thousands or hundreds of thousands of instances—and they can be multiplied that way—you can see how necessary and vital production is slowed. We do not want, we do not need, any more *snoopers* going around bothering the honest, patriotic citizens who are engaged in production to carry on the war. * * * * When does an agency not have someone on its staff who has, in his own mind, reason to suspect? Is there any agency which does not have some who think it their duty to suspect, to *snoop*, to show their authority. * * * * The purpose is to limit the 'snooping' that may be carried on under this bill which we do not have the votes to defeat." 97 Cong. Rec. 13377; emphasis supplied.

only the more limited question of the direct pertinence of certain categories of other costs—research and development, marketing and promotion, and distribution and administration costs—is presented here.

Bristol does not factor into its prices to the government, or, for that matter, even to its private vendees (including wholesalers),[7] any allowances for research and development expenses, marketing and promotion expenses, or those for general distribution and administration.[8] Yet, the government maintains that such costs "directly pertain to, and involve transactions relating to" the prices set in such government contracts.

Bristol sets its contract prices in the manner we shall detail immediately below, but decides what it can afford to spend on the above activities out of past and anticipated over-all revenues. (E.g., J.A. 132.) In short, it cuts the pattern of its research and development, marketing and promotional, distribution and administrative expenses to fit the cloth of its revenues, rather than weave revenue cloth to cover a desired pattern for such activities.

Bristol's contract prices are functions of its 1) manufacturing costs, such as raw and packaging materials, labor and fringe benefits, quality control and supervision; 2) manufacturing overhead, such as plant administration, production planning, warehousing, utilities and securities; 3) royalty expense; and, 4) in a general way, the cost of delivery to the sites specified in the contract. J.A. 107-08. Bristol would also probably consider competitive products

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[7] G.B. 33 n.17, 34 n.19. J.A. 133.

[8] J.A. 108, 126-27, 131-32. Bristol's accounting system does not identify any costs by groupings, by products, by classes of customers, or by government versus non-government contracts. J.A. 121-23, 129.

on pricing, and possibly look at other related products within its own division, their costs and prices. J.A. 120.[9]

The manufacturing costs referred to above are "standard" or "estimated" manufacturing costs (J.A. 120); that is, an estimate is made in August or September of a year as to what Bristol's raw material, packaging materials, labor, machinery costs and factory overhead costs are expected to be in the ensuing year. J.A. 122.[10] Differences between such forecast costs and ones actually incurred later are, for post hoc accounting purposes, aggregated as variances; they are not assigned, or allocated, to any particular products, sales or customers. J.A. 121-22, 125-26, 128-29.

III.

Fundamental principles of contract law preclude the Comptroller General from the access to Bristol's records he now seeks.

1. Unless a contrary intent by all parties is clearly shown, words in a contract are to be given their ordinary meaning.[11]

"[D]irectly" meaning "in a direct manner",[12] and "direct" meaning "characterized by close logical, causal or consequential relationship";[13] and "pertain" meaning "to belong

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[9] Also: J.A. 133-34, 137-38.

[10] "The estimate is based on what we expect that product to cost it in the year that it would be produced, the average cost during that year. Past history in some cases would be a factor in determining some of the components of that estimated cost." Ibid. Also: J.A. 121, 125.

[11] Restatement of the Law, Contracts, § 235(a).

[12] Webster's Seventh New Collegiate Dictionary, page 236 (G. & C. Merriam Company, 1972).

[13] Idem, page 235. "Without anyone or anything intervening; immediately." The Illustrated Heritage Dictionary and Information Book (Houghton Mifflin Company, 1977).

as a part, member, accessory or product . . . to belong as an attribute, feature, or function",[14] the combinations "directly pertain to" and "directly pertinent" mean, by their ordinary usage, that the cost records sought by the Comptroller General must, if he is to succeed, bear an integral relationship to the contracts at issue. That understanding, on which the parties to the contract are entitled to rely and to which they must be bound,[15] is augmented by the further explicit provisions that such costs must "involve transactions relating [or related] to" such contracts.

2. If there were any ambiguity inherent in the above-quoted contractual terms, it would have to be resolved against the Comptroller General, for the government is the contracting party that drafted and imposed them.[16]

In sum, as held by the courts below (Pet. App. 10a-11a):

> Although the access to records clause has its origins in statute, it is nevertheless a contractual provision. We are thus confronted with the task of construing the contracts, a task which turns on the intent and understanding of the parties regarding the import of the access to records clause at the time the contracts were entered. The government's position is particularly unrealistic when viewed in this light. It is inconceivable that Bristol, or any contracting firm, could have understood this clause to authorize the sweeping power of inspection claimed by the GAO. As a matter of contractual construction, the government's argument falls of its own weight.

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[14] Webster's supra, at page 631.

[15] District Court opinion, Pet. App. 10a-11a, aff'd., idem 3a.

[16] Restatement of the Law, Contracts, § 236(d); Corbin on Contracts, § 559.

3. Once bound to the terms of a contract, no party can by unilateral declaration alter them to its own benefit,[17] the very situation here (see G.B. 23-28).[18] While Bristol has not felt it necessary to rely upon the Comptroller General's attempt to employ his asserted right of access abusively, as have *amici*,[19] it can point out how incompatible such a motivation is with the congressional abhorrence toward his anticipated snooping that led to incorporation of "directly" into the statute (supra, page 5 at n.6).

IV.

Fundamental principles of statutory construction preclude the Comptroller General from the access to Bristol's records he now seeks.

To reverse the decisions of the courts below would require determination that despite congressional intention that the Hardy amendment not open the door to governmental snooping (supra, page 5 at n.6), that despite its intention not to "burden" the legislation with more than a restricted

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[17] Restatement of the Law, Contracts, § 230; Corbin on Contracts, § 538, n.50 and § 543, n.89.

[18] This governmental exercise is futile in any event. While agency interpretation of an ambiguous *statutory* (in contrast to a contractual) grant of authority may be entitled to judicial respect, even that does not apply where the language of the statute is clear, for to hold otherwise would defeat the legislative function. *Shea* v. *Vilpando*, 416 U.S. 251, 262, n. 11 (1974). The government attempts to hurdle this obstacle by enlisting the *Hewlett-Packard* decision as an implicit provision in its procurement contracts (G.B. 37). That avails it naught, for *Hewlett-Packard* dealt only with production costs, not with those of the quite different kind now in issue. Infra, pages 17-18.

[19] Reflected in *Eli Lilly & Co.* v. *Staats*, 574 F.2d 904, at 909-10 and (dissenting judge) 918-19 (7th Cir. 1978); Note, *Eli Lilly & Co.* v. *Staats:* An Undue Expansion of the GAO's Investigatory Power Under the Access-To-Records Statutes. 74 Northwestern University Law Review 122, at 125-30 (1979).

access right for the Comptroller General (supra, page 4, n.5), that despite its intention not to confer statutory power upon the Comptroller General but only to allow him such rights as the law of contracts permits (supra, pages 3-4), congress did intend to vest him with power to examine virtually every book and record of any firm entering into a supply contract with the government.[20]

Unless convinced that such was truly the legislative intent, this Court is, we respectfully submit, bound to affirm the decisions of the lower courts. *Tennessee Valley Authority* v. *Hill*, 437 U.S. 153, esp. 194-95 (1978).

V.

The government's arguments are unavailing.

The government's contentions run along seven lines. It relies upon: 1) 31 U.S.C. 53(a) (G.B. 8-9, 13, 23); 2) legislative history of the Hardy amendment (G.B. 9-11, 15-19, 30); 3) the Comptroller General's own interpretation of the Hardy amendment (G.B. 10, 23-28); 4) a bottom line theory, i.e., that because Bristol's expenditures for research and development, marketing and promotion, general distribution and administration must ultimately be met out of its total revenues, whatever their sources, and because payments by the government under the contracts involved here contributed to such total revenues, those costs must be deemed "directly pertinent to" and "involved in" such contracts (G.B. 34); 5) the *Hewlett-Packard* and *Lilly* decisions (G.B. 20, 30-31, 34-35); 6) a line of decisions exemplified by *Federal Crop Insurance Corp.* v. *Merrill*, 332 U.S. 380, 383-85 (G.B. 37); and, 7) sections of 41 C.F.R. (G.B. 35-36). These will be dealt with in that order.

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[20] District Court opinion, Pet. App. 9a-10a; adopted by Court of Appeals, idem at 3a; and infra, page 15, n.26.

1) 31 U.S.C. 53(a).

Not until this last, desperate moment has the government bethought itself to rely on this provision as *deus ex machina*. All through the proceedings in the district court, all through the court of appeals proceeding, even in its petition for a writ of certiorari herein, the government had evidently believed 31 U.S.C. 53(a) to be inapplicable.[21]

Plainly, that belief was shared by congress when it enacted the Hardy amendment. It is not to be presumed that congress was ignorant of the already existing section 53(a), or that it intended to indulge in mere redundancy. Congress could have had only one of two purposes in enacting the Hardy amendments: either to fill a gap left by section 53(a) (which would make it inapplicable here), or to cut back its authorization of the Comptroller General to the more restrictive limits of direct pertinency prescribed by the Hardy amendments. In either event, it is the contractual provisions specified by those amendments that control; they are specific, contrasted with section 53(a)'s generality, and they postdate it.

2) Legislative history, and

3) The Comptroller General's interpretations.

Legislative history supports Bristol's position rather than the government's (supra, pages 3-5) as do the Comptroller General's expressions (G.B. 23-28). The references specifically relied upon by the government demonstrate that congress intended by the Hardy amendments to protect the government against improprieties in the negotiation of government procurement contracts.

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[21] In *Lilly*, although, as here, the Comptroller General had initially made a boilerplate reference to 31 U.S.C. 53 and 67 (J.A. 38), the government rejected the sections under the test of litigation. 574 F.2d at 910.

Even if, as the government contends, the access clauses were intended to permit the Comptroller General to assess the reasonableness of Bristol's prices, Bristol's omission from its computation of prices to the government of any allowance for the costs at issue could not contribute to waste, extravagance, excessiveness, unreasonableness or impropriety in its prices;[22] quite the contrary. Excluding particular cost items from the computation of prices can only lower them. It would be only the increasing of prices to the government by adding such costs to their base that could raise questions as to excessiveness, waste, unreasonableness, unfairness or impropriety.

No harm can be done to the Comptroller General's asserted interest to monitor the reasonableness of Bristol's prices to the government if data concerning such expenses remain unavailable to him. Inquiry by the Comptroller General into costs that have been excluded as pricing factors, on an unsubstantiated assertion that they are somehow "directly pertinent" to the transactions at bar, could only enhance, not impugn, the fairness of Bristol's prices. Absent reliance upon such costs as justification, Bristol's prices to the government stand in their poorest light of reasonableness. If the Comptroller General might find additional expenditures that could have been assigned to the subject transactions, but were not, that would only make Bristol's prices more reasonable and fair by reducing its gross profit on them. One may doubt that the Comptroller General's interest is in demonstrating that contractors' prices are less excessive and more protective of the government's interests (supra) than they facially seem, due to failure to assign properly allocable costs to their validation.

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[22] Even the Comptroller General's own interpretations upon which the government relies, would, at most, go no further than access to protect against such improprieties as these. G.B. 11, 16, 20-25, 27, 30-31, 33, 34 and their pertinent footnotes.

The statement by General Counsel of GAO, Robert Keller, Esq. (G.B. 26) speaks only to his perceived need for the agency to obtain "cost data to support price proposals and quotations". Bristol's withheld costs were not additions in reaching its contract prices. Data concerning them are, therefore, not necessary, or even pertinent, "to support" their "proposals and quotations".

In like vein is the statement of GAO's Assistant General Counsel, Paul Shnitzer, Esq. (G.B. 27-28). Even under his expansive interpretation, he makes clear that only the "costs . . . actually incurred in the performance of the contract", and those "generated in the performance of that contract . . . how much it cost him to perform that contract" define the appropriate area of concern for the Comptroller General to access a contractor's records. Bristol's expenses for research and development, marketing and promotion, and distribution and administration were not "incurred in the performance of the contract[s]" at issue here, were not "generated in [their] performance", and were not costs in order for Bristol "to perform those contracts" (supra, pages 6-7).[23] They would be incurred and generated regardless of the contracts in issue here. E.g., J.A. 131-32.

Apart from that, the government's own references to statements by Representatives Harvey and Hoffman demonstrate that even they, with their fears of governmental snooping, did not perceive the Hardy amendments, even

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[23] Even if Mr. Keller were correct in stating "that GAO could 'go beyond direct manufacturing costs' into such areas as 'how research costs are allocated as between the Government contract and commercial business' " (G.B. 26), that information has already been supplied to the Comptroller General by Bristol: namely, there is no such allocation in setting prices to either government or non-government customers, such pricing being posited primarily upon standard manufacturing costs, manufacturing overhead, royalty expense, competition, and the costs and prices for other of Bristol's related products (supra, pages 6-7). That such, and such alone, are the "directly pertinent" costs is further confirmed by regulations cited by the government itself (infra, page 21).

before addition of the restricting modifier "directly", as extending to unallocated costs (G.B. 18).[24]

In light of *Hewlett-Packard's* holding having not dealt with the costs involved in Bristol's refusal of access to the Comptroller General (infra, pages 17-18), and of the legislative and GAO's own concern having been focused on improper pricing (supra, pages 11-12), a concern which cannot be frustrated by such denial of access (supra, page 12), the government's contention that Bristol should be bound by its contracts to grant the access (G.B. 37) rings hollowly.

It may well be noted that Representative Hardy undertook to assuage the trepidations of the supporters of the Harvey amendment by stating, "I tried to state this many times, that we are not anticipating that the General Accounting Office could possibly go into all of these things, but they would have the right to do it if they had any reason to suspect fraud or bad faith or illegality." (97 Cong. Rec. at 13377, col. 2.) No such "reason to suspect" has been suggested by the government here.

4) The government's bottom line theory.

Undoubtedly, to remain solvent Bristol must over some span of time ultimately recover from total revenues its total expenses. So, too, must every business enterprise. "[D]irectly", and even "pertain", in the Hardy amendments would be sterile in meaning if because of that Bristol's out-

[24] It was undoubtedly their concern, and that of the other representatives who voted for the Harvey amendment (97 Cong. Rec. at 13377), that led to the *subsequent* proposal and adoption of Representative Hoffman's amendment adding "directly" to constrict "pertinent". The strength of their concern, of which Representative Hardy was certainly well aware, negates that adding "directly" was intended not to "sharply narrow[ ] the scope of inquiry to be allowed the GAO" simply because he agreed so readily to including it (G.B. 19).

lays for research and development,[25] advertising and promotion, and general administration and distribution were to be deemed "directly pertinent to" and related to the contracts at issue here, despite the fact that Bristol did not include any costs of such "transactions" in its formulation of the prices for such contracts. Congress might just as well have written that the Comptroller General should have access to records of every "transaction" impacting upon the profit and loss statements and balance sheets of every contractor supplying federal agencies.[26]

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[25] Research and development expenses are not allocated to particular products for good reason. They do not relate to products that are currently being sold, but rather involve *projects* that may *or may not* develop into products sometime in the future. J.A. 131-32.

[26] "The United States insists that the GAO may inspect Bristol's records with respect to any and all costs met in whole or in part from revenues earned on the federal contracts, whether or not those costs are specifically assigned by Bristol to the contracts or the products delivered. According to the government the test is simply 'whether the burden of [the] costs is borne by the Government in the prices it must pay for the contract items.' . . . . The Government's theory has far reaching implications. The only items excludable from the Comptroller General's reach would be those, if any, which relate to the costs recovered exclusively from non-government contracts. . . . It is undisputed, however, that Bristol does not separately compute the cost of government and non-government contracts or pay for them out of separate funds. Accordingly, there are no excludable records under the Government's theory. . . . If the government's interpretation of the access to records clause is correct, Bristol will be required to make available virtually all of its books and records, because although it is impossible to trace the use of government dollars, those dollars contribute to the fund from which all of the company's expenses are paid.

Such a result would be inconsistent with the language of the access to records clause and the statutes pursuant to which the clause was included in the contracts. . . . It is a distortion of the language to argue that it permits GAO officials to discover virtually everything there is to know about the structure of the contractors' business. The reasonable assumption is that if Congress had wished to condition the receipt of a fixed-price negotiated contract on the contractors' agreement to allow such unusual and unfettered government inspection of their business records, it would have done so explicitly." Lower court decisions, Pet. App. 9a-10a, 3a.

An equivocal word invades the government's brief, confusing its arguments: "allocate".[27] There are two places in Bristol's operation at which allocation of costs can take place. The first is pre-contract, where certain costs are employed in the negotiating process as factors in determining the price to be charged in the contract; records of such costs would be directly pertinent to such contracts, and Bristol has granted the Comptroller General access to them. The second spot, however, is in Bristol's post hoc accounting procedure, whereby it retrospectively analyzes its financial circumstances and the relationships of its various activities in them.

The government's confusion of these different kinds of allocation underlies its assertion that Bristol cannot affect the Comptroller General's right to access by its own choice of accounting methods.[28] We agree; but that cuts both ways. As Bristol's accounting methods cannot detract from the Comptroller General's right of access, neither can they add to it.

The government's argument might be valid "[i]f respondent had fully allocated its costs" to *arrive at* the prices charged in its contracts at issue; then GAO's right of access might be clear. G.B. 33. But a post hoc accountancy allocation of cost items that played no role in arriving at the contract prices, not being "directly perti-

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[27] E.g., G.B. 33-36.

[28] ". . . [T]he government cannot be bound by the accounting method respondent has established for its own purposes. . . . If respondent had fully allocated its costs, GAO's right to conduct an inspection adequate to evaluate the reasonableness of the contract price would be clear. No different outcome is warranted simply because respondent has chosen to allocate only some of its costs to particular contracts or products. Indeed, the logical consequence of the court of appeals' decision is that respondent would not be obliged to open any of its books to the Comptroller General if, for internal bookkeeping purposes, it chose to allocate none of its costs to a particular contract or product." G.B. 33.

nent" to setting them, would not give rise to a right to access he did not otherwise have.

In any event, Bristol did not make even such post hoc accounting allocations to the government contracts at issue of the transactional costs involved here.[29]

5) *Hewlett-Packard* and *Lilly*.

Bristol has from the outset agreed to provide the Comptroller General with cost records of the type *Hewlett-Packard* ruled upon; namely "costs of direct material, direct labor and overhead costs in producing the items furnished under the contracts" (385 F.2d at 1015), "the cost of producing the items furnished by Hewlett-Packard Company under the aforesaid contracts, including costs of direct material, direct labor and overhead costs." (idem at 1016), and "[p]roduction costs . . . in obtaining the materials, labor, facilities and the like required by [Hewlett-Packard] in fulfilling its commitment with reference to the subject matter of the contract." Ibid. That case did not rule upon the kinds of costs Bristol, and the lower court, assert lie beyond the Comptroller General's right of access: namely, research and development, advertising and promotion, and, in general, administration and distributional costs that Bristol has not utilized to compute its prices to the government.

Nonetheless, the government relies upon an unsubstantiated declaration in *Lilly* that *Hewlett-Packard* established a broad reading of the "directly pertinent" phrase, broad enough to encompass the types of costs that *Hewlett-Packard* never discussed or ruled upon. 574 F.2d at 913. The *Lilly* court offers no identification of such a "broad reading", satisfying itself solely with its *ipse dixit*.[30] The

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[29] J.A. 113, 122-24, 126-32, 136-37, 139-40.

[30] The *Lilly* court's own "reading" of "directly pertinent" turns upon a criterion that finds no support in either the history or the

broadness of *Hewlett-Packard*'s reading was no more than that even though, in that case, production costs were not taken into consideration in fixing the contract prices (catalog prices were used), they "directly pertain to [the contract's] subject matter, because if such *production* costs were out of line with the contract price, the contract may have been an inappropriate means of meeting this particular procurement need of the Government." 385 F.2d at 1016; emphasis supplied. Whether or not the *Hewlett-Packard* decision was correct, Bristol has not sought to withhold production costs records from the Comptroller General. G.B. 5.

In essence, the *Lilly* majority accepted the government's bottom line theory. Under it there would appear to be no expense in the total firm picture that would be merely pertinent; none that could be pertinent without being "directly" pertinent. In effect, it would read the Hoffman amendment out of the Hardy amendments.

It is no wonder that no more than a year later two of the three judges in *United States* v. *Abbott Laboratories*, 597 F.2d 672 made clear that they would have decided *Lilly* the other way, and that they held as they did in *Abbott* only because of the constraint of *stare decisis*. Idem at 674-75. One of those judges (Judge Pell) had been the dissenting judge in *Lilly*, 574 F.2d at 918-19. In *Abbott* he reiterated his opinion that "[t]he Comptroller General, giving what I regard as a fair reading to his demands, goes

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language of the Hardy amendments, and certainly not in *Hewlett-Packard;* namely, the ratio of production to non-production costs. Idem at 913-14. Such a rationale would presumably entitle the Comptroller General to access all a firm's expenses so as to satisfy himself as to what the relativity is between the two types of costs in all its operations, governmental and non-governmental. Thus, there would be no record to which his scrutiny could be barred if the *Lilly* rationalization is to be credited.

far beyond 'directly pertinent books, documents, papers, and records.'" 597 F.2d at 675.

Thus, a change of but one judge on the *Lilly* panel could well have resulted in an opposite decision, hence in *Abbott* as well, which would have left no diversity among circuits regarding the kinds of costs, and their lack of incorporation into pricing formulations, to support granting the writ of certiorari herein. Pet. App. 8-9. However viewed, the *Lilly* majority's rationalization is watery support for the government's position here.

6) The *Federal Crop Insurance Corporation* v. *Merrill* line of decisions.

These cases hold simply that a validly enacted administrative regulation, promulgated within delegated authority, conditions the terms of a contract entered into by that agency, even though not explicitly incorporated in it. All parties are bound; the governmental agent cannot vary it, and the private contractor cannot deny knowledge of its existence or controlling effect.[31] The within case involves

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[31] "Whatever the form in which the Government functions, anyone entering into an arrangement with the Government takes the risk of having accurately ascertained that he who purports to act for the Government stays within the bounds of his authority. The scope of this authority may be explicitly defined by Congress or be limited by delegated legislation, properly exercised through the rule-making power. And this is so even though, as here, the agent himself may have been unaware of the limitations upon his authority." *Federal Crop Insurance Corp.* v. *Merrill*, 332 U.S. 380 at 384. "As such regulations were issued pursuant to statutory authority (39 U.S.C. §401), they have the force and effect of law, and, if they are applicable, they must be deemed terms of the contract even if not specifically set out therein, knowledge of which is charged to the contractor." *De Matteo Construction Company* v. *United States*, 600 F.2d 1384 at 1391. "It is well settled that Regulations of an Executive Department have the force and effect of law. [Citation.] The law in effect when a Government contract is made becomes a part of the contract. . . . Consequently, these

no issue as to the binding effect upon a contracting party of a duly authorized and promulgated administrative regulation. There is no such regulation.

This case is governed by explicit clauses in the contracts at issue. They were enacted by the congress, not promulgated by the Comptroller General. The issue here is only as to the meaning to be given such provisions, and their consequent enforcement upon the government as well as upon Bristol. The Comptroller General has not been authorized unilaterally to vary them either within the contracts themselves or externally by regulation; much less by self-serving declarations "interpreting" them.

7) 41 C.F.R.

Equally fruitless is the government's implication of Federal Procurement Regulations. The 41 C.F.R. 1-3. series does no more than codify definitions for certain terms as used in standards for cost accounting.[32] Except to the

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Regulations were a part of the plaintiff's enlistment contract and required him . . . [etc.]". *Jackson* v. *United States,* 573 F.2d 1189 at 1194. "[W]e hold that, in the procurement field as in others, an authorized regulation can impose such peremptory requirements on federal officials and those who seek to enter into transactions with the Government." *G. L. Christian and Associates* v. *United States,* 320 F.2d 345 at 351. *United States* v. *Wunderlich,* 342 U.S. 98, held only that a party entering into a contract with the government and agreeing to a clause that granted the latter arbitral powers for the settlement of any dispute was bound to that commitment and could not complain about any decision made by the government absent a finding of fraud. "Respondents were not compelled or coerced into making the contract. It was a voluntary undertaking on their part. As competent parties they have contracted for the settlement of disputes in an arbitral manner. This, we have said in [citation], Congress has left them free to do. [Citation.] The limitation upon this arbitral process is fraud, placed there by this Court." Idem at 100.

[32] "Definitions promulgated by the Cost Accounting Standards Board are set forth herein. Unless the text of a particular stan-

extent that a definition may carry with it substantive consequences, the series 1-3. regulations have no law-making intendment. Insofar as 41 C.F.R. 1-15.201-4 and 1-15.205-35 are concerned, they allow, but do not require, contractors to allocate certain indirect costs in arriving at a price to the government. They do not apply where the contractor elects not to do so; hence have no bearing here.[33]

If anything, the Federal Procurement Regulations lean in Bristol's direction, rather than the government's, by clearly distinguishing between direct and indirect kinds of costs (analog: "directly pertinent" versus "indirectly pertinent").[34]

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dard demands a different definition or the definition is expressly modified for a particular standard, terms defined herein whenever used in any standard shall have the meanings ascribed to them in this paragraph (b)." 41 C.F.R. §1-3.1220(b).

[33] 41 C.F.R. §1-3.1220(b)(24) defines *"Pricing"* as "The process of establishing the amount or amounts to be paid in return for goods or services." Bristol elected not to include its costs for the activities now at issue in "establishing the amount or amounts to be paid in return for [its] goods". Not being involved in the pricing, they are, therefore, not directly pertinent to it.

[34] *"Direct cost. . . .* Costs identified specifically with a contract are direct costs of that contract. All costs identified specifically with other final cost objectives of the contractor are direct costs of those cost objectives." 41 C.F.R. §1-3.1220(b)(7). *"Final cost objective.* A cost objective which has allocated to it both direct and indirect costs, and, in the contractor's accumulation system, is one of the final accumulation points." Idem §1-3.1220(b)(11). *"Indirect Cost.* Any cost not directly identified with a single final cost objective, but identified with two or more final cost objectives or with at least one intermediate cost objective." Idem §3.1220(b)(14) (The very kinds of costs in controversy here!).

CONCLUSION

The judgment below should be affirmed.

Respectfully submitted,

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March, 1981

No. 80-264

1981

In the Supreme Court of the United States

OCTOBER TERM, 1980

ELMER B. STAATS, COMPTROLLER GENERAL OF THE UNITED STATES,

AND

UNITED STATES OF AMERICA, PETITIONERS

v.

BRISTOL LABORATORIES DIVISION OF BRISTOL-MEYERS COMPANY

ON WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE SECOND CIRCUIT

REPLY BRIEF FOR THE PETITIONERS

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In the Supreme Court of the United States

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ELMER B. STAATS, COMPTROLLER GENERAL OF THE UNITED STATES,

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REPLY BRIEF FOR THE PETITIONERS

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1. a. Respondent principally argues (Resp. Br. 3-4, 7-9, 20) that, under principles of contract law, the access-to-records clause should be construed to be inapplicable to the cost records at issue in this case. As discussed in our opening brief (Pet. Br. 3-4, 37), however, the clause was required to be included in the contracts by 10 U.S.C. 2313(b) and 41 U.S.C. 254(c),

and its meaning is necessarily determined by those statutes rather than by the intentions of the parties. Where a statute directs that a contract contain a specified provision, such a statute is, as Professor Corbin has explained,

> one that prescribes the legal operation of contracts, not one that affects factual interpretation. If in exact obedience to the law, the specified provision is integrated into a written contract in exact terms, the provision must be interpreted and given effect in accordance with the intention of the legislature, irrespective of how the contractors understood it. Exactly the same result is reached even though the parties know nothing of the statute and do not include the provision, and even though they know of it and expressly agree upon the exact contrary.

3 A. Corbin, *Contracts* § 551, at 200-201 (1960) (footnotes omitted). Thus, the maxims of contract construction cited by respondent are simply inapposite here.[1]

b. With respect to 10 U.S.C. 2313(b) and 41 U.S.C. 254(c), respondent contends (Resp. Br. 11) that the Comptroller General's construction would make the access statutes redundant with 31 U.S.C. 53(a), which provides that "[t]he Comptroller General shall investigate * * * all matters relating to the receipt, disbursement, and application of public funds" and

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[1] Respondent's attempt (Resp. Br. 19-20 & n.31) to distinguish the authorities relied on in our brief (Pet. Br. 37) is wholly unpersuasive. Indeed, the fact that the access clause in the contracts was required by statutes rather than administrative regulations serves, if anything, to reinforce the conclusion that the meaning of the clause turns not on the agreement of the parties but on the construction of the legislation.

"shall make recommendations [to Congress] looking to greater economy or efficiency in public expenditures." However, as we discussed in our opening brief (Pet. Br. 13), 31 U.S.C. 53(a), while not a source of authority for GAO to inspect contractors' records, is part of the background and context in which the access provisions were enacted. And, contrary to respondent's assumption, Sections 2313(b) and 254(c) were designed precisely "to fill a gap left by section 53(a)" (Resp. Br. 11). See Cibinic & Lasken, *The Comptroller General and Government Contracts*, 38 Geo. Wash. L. Rev. 349, 388 (1970):

> While the 1921 and 1950 Acts [which include 31 U.S.C. 53(a)] are broad enough to support the Comptroller General's audits of Government contracts, they give him no right to examine the books and records of Government contractors. This was remedied by statute and now all negotiated contracts are required to contain [access-to-records] clauses * * *.

Relying on the addition of the word "directly" to the access provisions introduced by Representative Hardy, respondent contends (Resp. Br. 3, 5, 13-14 & n.24) that Congress intended to be "miserly" (*id.* at 2) and "parsimonious" (*id.* at 3) with the access authority provided to the Comptroller General. For the reasons previously discussed (Pet. Br. 19), we do not believe that this amendment, to which Representative Hardy readily agreed, should be read to effect a significant contraction of the Comptroller General's right of access or to exclude records that are legitimately needed to determine the reasonableness of the contract price. To accept respondent's argument, in light of the legislative history set out in our opening brief, " 'would be to impute to Congress a purpose to

paralyze with one hand what it sought to promote with the other.'" *Weinberger* v. *Hynson, Westcott & Dunning*, 412 U.S. 609, 631 (1973), quoting *Clark* v. *Uebersee Finanz-Korp.*, 332 U.S. 480, 489 (1947).

Respondent also contends (Resp. Br. 7-8) that the plain meaning of the term "directly pertinent" in the access-to-records provisions demonstrates that the records of non-manufacturing costs are not subject to GAO examination. However, "[a]s in all cases of statutory construction, our task is to interpret the words of these statutes in light of the purposes Congress sought to serve." *Chapman* v. *Houston Welfare Rights Organization*, 441 U.S. 600, 608 (1979). See also, *e.g.*, *FTC* v. *Fred Meyer, Inc.*, 390 U.S. 341, 349 (1968) ("we cannot, in the absence of an unmistakable directive, construe the Act in a manner which runs counter to the broad goals which Congress intended it to effectuate"). Here, the evident congressional purpose was to enable the Comptroller General to examine all of a contractor's cost records that are necessary and appropriate to determine whether the price charged the government was "extravagan[t]," "excessive," or "wasteful[]." 97 Cong. Rec. 13198 (1951) (remarks of Rep. Hardy). Respondent's reading is inconsistent with this remedial purpose and must be rejected.

Moreover, as commonly understood, "direct" means "[i]n the usual or natural course * * *. In the usual or regular course or order * * *. The opposite of * * * collateral or remote." *Black's Law Dictionary* 413 (5th ed. 1979). Similarly, "pertinent" is defined as "[a]pplicable; relevant" (*id.* at 1030). The cost records at issue here are manifestly not "collateral or remote" or "[ir]relevant" to the reasonableness of the contract price, and they fall well within the literal terms of the access provisions. As the court of ap-

peals explained in *Eli Lilly & Co.* v. *Staats*, 574 F.2d 904, 914 (7th Cir.), cert. denied, 439 U.S. 959 (1978):

> [R]esearch and other costs not immediately attributable to one product form such a large portion of the costs of a pharmaceutical product that their import to such a contract seems inescapable. * * * [C]osts such as research and development at the least appear to have a logical, causal and consequential relationship to a portion of the price of the products purchased by the Government. Further, contrary to plaintiff's contention, such costs are not "remote" within the established definitions of that term in relation to at least a portion of the price because their inclusion in the price of the product is not unforeseeable once the costs are incurred, nor is their impact on a part of the price significantly altered by any intervening cause. * * * Thus in relation to the contract as a whole, these costs fit within the common and legal understandings of "directly pertinent." The mere fact that, as plaintiff asserts, it does not or even could not allocate costs such as research and development to an individual contract does not undercut the proposition that those costs are directly pertinent to an individual contract but merely indicates that they are directly pertinent to more than one individual contract.

Respondent further submits (Resp. Br. 12) that exclusion of its non-manufacturing costs from consideration by GAO would necessarily work to the company's disadvantage and therefore would not interfere with the Comptroller General's responsibility to assess the reasonableness of the contract price to the

government. However, in light of the substantial nature of non-manufacturing costs in the pharmaceutical industry (see Pet. Br. 31-33) and the fact that the government was charged respondent's normal wholesale price (*id.* at 34 n.19), it is specious to suggest that GAO could make a determination of the reasonableness of the contract price without regard to such significant unallocated costs as research and development, advertising and promotion, distribution, and administration. Furthermore, notwithstanding respondent's "doubt[s] that the Comptroller General's interest is in demonstrating that contractors' prices are less excessive and more protective of the government's interests * * * than they facially seem" (Resp. Br. 12), it is unquestionably important to GAO to learn whether the present system of negotiated procurement adequately protects the government's interests. Likewise, if the contract price was unreasonable and the negotiation procedures inadequate, it is important to determine the amount of the excessive price and the degree of the inadequacy. Only in this way, by being fully informed of the advantages and disadvantages of negotiated procurements, can the Comptroller General properly discharge his statutory responsibility to study the advisability of reform and to recommend "other methods of meeting future procurement needs." *Hewlett-Packard Co.* v. *United States*, 385 F.2d 1013, 1016 (9th Cir. 1967), cert. denied, 390 U.S. 988 (1968).[2]

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[2] Respondent's entire argument has failed to identify any congressional purpose expressed in the legislative history of the access statutes, or any sound reason of federal procurement policy, that would support its position in this case. On the contrary, the limited access allowed GAO under respondent's rigid and procrustean interpretation provides for no

Respondent also appears to suggest that the access-to-records provisions were intended by Congress only to protect the government against "improprieties in the negotiation of government procurement contracts" (Resp. Br. 11), "improper pricing" (*id.* at 14), or "'fraud or bad faith or illegality'" (*ibid.*, quoting 97 Cong. Rec. 13377 (1951) (remarks of Rep. Hardy)). This would represent a marked departure from respondent's previous position in the litigation, which has consistently conceded the Comptroller General's right to examine records in the absence of a suspicion of such improprieties and has acknowledged that "[t]he driving motivation of the [C]ongress was to empower the Comptroller General to audit governmental contracts' costs and performance to the end that the government be guarded against excessive cost or waste. The listing [of legislative history] recited in the Petition resounds with that dominant, if not singleminded, purpose" (Br. in Opp. 9). In addition, respondent expressly disclaims this position elsewhere in its brief (see Resp. Br. 5-6, 9, 18).

We doubt that this argument, if in fact it is being advanced by respondent, is properly before the Court. The question presented in our petition concerns GAO's right of access to a contractor's records of unallocated costs that are defrayed by the government's payments under the contract. The issue of whether GAO's entitlement to records depends on suspicion of improprieties is plainly not a "subsidiary question fairly included therein." Sup. Ct. R. 21.1(a). Moreover, this argument would be inconsistent with the judg-

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meaningful review by the government and is completely divorced from any procurement objective that the access provisions could be thought to serve.

ment below (Pet. App. 15a-17a), which allows GAO access to designated records even though there was no allegation or suspicion of impropriety, and therefore it cannot be urged as an alternative ground for affirmance of the judgment. See, *e.g.*, *FEA* v. *Algonquin SNG, Inc.*, 426 U.S. 548, 560 n.11 (1976). As the Court recently explained in *Andrus* v. *Idaho*, 445 U.S. 715, 725 n.6 (1980), "respondent is not entitled, absent a cross-petition, to bring that issue before us; for a favorable ruling would enlarge the relief granted the [respondent] under the Court of Appeals judgment." Since respondent did not cross-petition for certiorari, it should not be heard to raise this issue.[3]

At all events, for the reasons stated in our opening brief (Pet. Br. 15-30) and in our brief in opposition (at 7-17) in *SmithKline Corp.* v. *Staats*, conditional petition for cert. before judgment denied, No. 80-434 (Dec. 8, 1980), the argument that access is limited to the detection of fraud is without merit.[4]

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[3] In addition, since this issue was not presented in the courts below, respondent cannot properly press it here. See, *e.g.*, *United States* v. *Mitchell*, 445 U.S. 535, 546 n.7 (1980). Indeed, as noted in the text, respondent has deliberately declined to argue this position and has "agree[d] that it is obliged by the terms of the contracts to provide access to records of [certain of its costs] * * *" (Pet. App. 8a).

[4] See also *Hearings on Comptroller General Reports to Congress on Audits of Defense Contracts before the Subcomm. on Military Operations of the House Comm. on Government Operations*, 89th Cong., 1st Sess. 577, 639, 649-653 (1965) (statement of Acting Comptroller General Weitzel); H. Wright & J. Bedingfield, *Government Contract Accounting* 150 (1st ed. 1979) ("GAO's audit responsibility is much broader [than that of the procurement agency], usually

c. Respondent asserts (Resp. Br. 10, 15) that the Comptroller General seeks access to virtually all of its books and records. To the extent that broad access is required here, it is, as noted in our opening brief (Pet. Br. 33-35 & n.20), made necessary by the way in which respondent has chosen to maintain its records.

Moreover, the access sought in this case is not nearly so extensive as respondent portrays. First, GAO's request was limited to cost and pricing records. Second, the only material in dispute is confined to records of costs that are a normal and integral part of respondent's pharmaceutical business and constitute significant expenditures in the drug industry (see Pet. Br. 31-33)—in particular, records pertaining to costs of research and development, advertising and promotion, distribution, and administration.

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being directed toward determining the economy and efficiency of the overall procurement process").

Congress has recently reiterated its concern that the Comptroller General have adequate and timely access to contractors' records in order to assess the economy and efficiency of government expenditures. In Pub. L. No. 97-226, Section 102, 94 Stat. 313 (to be codified at 31 U.S.C. 54(c)), Congress authorized the Comptroller General to issue subpoenas if necessary to obtain the books and records "of contractors, subcontractors, or other non-Federal persons to which he has access by law or by agreement of the non-Federal person from whom access is sought." The Committee Reports on the Act emphasize that "this legislation is intended to strengthen the General Accounting Office's ability to discharge its functions as an investigative and auditing arm of the Congress. * * * Congress relies both on the GAO and on the Comptroller General to ensure that * * * agency resources are managed efficiently and economically * * *." S. Rep. No. 96-570, 96th Cong., 2d Sess. 1 (1980); H.R. Rep. No. 96-425, 96th Cong., 1st Sess. 1 (1979).

Thus, GAO has made no attempt to inspect records of costs that are peripheral or inconsequential. Finally, although no examination of respondent's records has yet occurred, GAO has generally found that government contractors maintain certain records—such as summaries for supervisory or management personnel, periodic budget or accounting statements, or monthly, quarterly, or annual reports—that render unnecessary a detailed review of much of the underlying documentation concerning day-to-day transactions.

To be sure, GAO access must be thorough and comprehensive, and many documents will need to be examined because of respondent's record-keeping system. However, it appears that respondent greatly exaggerates the scope of the inspection that is likely to be conducted in this case. GAO seeks no broader access than is necessary and appropriate to determine the reasonableness of the price charged the public fisc by those who elect to do business with the government.[5]

2. a. Amici Merck & Co. and SmithKline Corporation, purportedly filing "in support of the judgment of the Second Circuit" (Am. Br. 1), frame the issue in this case to be "the scope of the Comptroller General's access-to-records authority" (*id.* at 4; see also *id.* at 5). Seeking to "place[] before the Court what *amici* consider to be the proper interpretation of the scope of the access-to-records statutes" (*id.* at 4),

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[5] Respondent cryptically relies (Resp. Br. 20-21) on the Federal Procurement Regulations in 41 C.F.R. ch. 1. Although respondent emphasizes (Resp. Br. 21 n.34) that "indirect costs" are "[t]he very kinds of costs in controversy here," nowhere does it reply to the argument (Pet. Br. 36) that a cost, including an indirect cost, is "allocable to a Government contract if it * * * [i]s necessary to the overall operation of the business, although a direct relationship to any particular cost objective cannot be shown." 41 C.F.R. 1-15.201-4.

amici contend that "no cost records of these contractors come within the scope of the access provision" because the contracts were "fixed-price rather than cost-based" and "there was no actual negotiation of prices" at the time the contracts were executed (*id.* at 7-8).

In our view, this is a highly improper submission by amici. Contrary to their characterization, the issue in this case is not whether any records are subject to the access provision, but rather whether the particular cost records withheld by respondent are within GAO's right of access. Indeed, amici expressly acknowledge (Am. Br. 4) that "[t]he position advanced by respondent Bristol in this case * * * is narrower than that presented by [amici] * * *."[6]

For the reasons already stated (see pages 7-8, *supra*), this issue would not be properly before the Court on our petition here even if it were raised by respondent, and certainly it is inappropriate for amici to interject the question into the case. See *Bell* v. *Wolfish*, 441 U.S. 520, 531-532 n.13 (1979); *Knetsch* v. *United States*, 364 U.S. 361, 370 (1960).[7] Moreover, both amici filed petitions for a writ of certiorari before judgment in order to present this argument to the Court, but their petitions were denied. See *Merck & Co.* v. *Staats*, conditional petition for cert. before judgment denied, No. 80-416 (Dec. 8, 1980), and *SmithKline Corp.* v. *Staats*, conditional petition for cert. before judgment denied, No. 80-434 (Dec. 8, 1980). Having failed to persuade the Court to hear their claim, amici should not now be allowed

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[6] Respondent, too, has recognized that amici urge a position far broader than its own (Resp. Br. 5-6).

[7] Amici also repeatedly find it necessary to go outside the record in this case and refer to the records in their own cases as support for the arguments they offer here.

to raise the same issue in the guise of supporting the judgment below.[8]

In light of these considerations, the Court should disregard this contention of amici.

b. Amici advance several arguments that, while directed to the foregoing issue, may be read to bear on the question presented in this case. Accordingly, we shall briefly respond to these points.

Amici argue (Am. Br. 12-14) that the legislative history of the 1951 amendment to the First War Powers Act,[9] which was substantially similar to the access provisions at issue here, indicates that 10 U.S.C. 2313(b) and 41 U.S.C. 254(c) should be narrowly construed. Similarly, they argue (Am. Br. 20-21) that GAO's contemporaneous construction of the access provisions, which refers to the history of the War Powers Act amendment, contradicts its position here. Neither of these arguments is correct.

Nothing in the language or history of the First War Powers Act casts doubt on our argument that respondent's records of unallocated costs are subject to GAO examination. To the contrary, Representative Celler explained that "[t]he import of the amendment is to give to the General Accounting Of-

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[8] In addition to this issue of statutory construction, amici's petitions also urged that the Comptroller General's requests for access were invalid on the ground that they were assertedly motivated by an improper purpose. Although professing to recognize that this question is not presented by the petition in this case (Am. Br. 5), amici argue precisely this point later in their brief (*id.* at 25-26). Once again, this discussion is improper; at all events, it is without merit for the reasons stated in our brief in opposition (at 11-12 & nn.8-10) in *SmithKline Corp.* v. *Staats*, *supra*.

[9] See Act of Jan. 12, 1951, ch. 1230, 64 Stat. 1257, amending 50 U.S.C. App. (1946 ed.) 611, repealed, Pub. L. No. 89-554, Section 8(a), 80 Stat. 651.

fice power of investigation and the right of access to all records and to examine all data of any firm * * * [subject to the statute]." 96 Cong. Rec. 17123 (1951).[10] In addition, Representative Hardy, the sponsor of the amendment, observed that the statute would afford "protection" for the government's interest by enabling "the Congress to review or have any action taken to audit [the contract]. If we can get this far we can get action by the Comptroller General and a report to Congress of what he then finds (*id.* at 17045).[11] Representative Hardy also stated that the Act would provide a "deterrent that we did not have under the [existing] law" (*ibid.*), and Representative Celler reiterated that "[t]he power of investigation and inquiry of the General Accounting Office should be an excellent deterrent" (*id.* at 17123).[12]

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[10] This characterization is later repeated in the legislative debates on Sections 2313(b) and 254(c). See Pet. Br. 17-19.

Amici object (Am. Br. 19) that our previous discussion of the legislative history relies in part on statements of opponents of the Hardy bill. This Court has recognized, however, that while "statements of opponents of a bill may not be authoritative, * * * they are nevertheless relevant and useful, especially where, as here, the proponents of the bill made no response to the opponents' criticisms." *Arizona* v. *California*, 373 U.S. 546, 583 n.85 (1963). See also, *e.g.*, *First National Bank of Logan* v. *Walker Bank & Trust Co.*, 385 U.S. 252, 261 (1966).

[11] The legislative history of the subsequent access-to-records provisions echoes this view of the purpose of the statute. See Pet. Br. 17.

[12] As Representative Hardy stated in connection with Sections 2313(b) and 254(c):

> [M]y main purpose in offering this bill was to place on the statute books a law which will act as a deterrent to improprieties in the negotiation of Government contracts. It would be impossible for GAO to inspect even a major

And, on several occasions, concern was expressed that the exigencies of the Korean War might give rise to inordinate profits, the result of excessive pricing having no relationship to fraud on the part of the contractor. See, *e.g.*, 96 Cong. Rec. 17046 (1951) (remarks of Rep. Marcantonio); *id.* at 17124 (remarks of Rep. Reed). This history is fully compatible with our interpretation of Sections 2313(b) and 254(c).

In a statement heavily emphasized by amici (Am. Br. 13-14), Representative Celler further noted that "[t]he amendment will give power to the General Accounting Office to go into the books and delve into the records of these contractors * * * to determine whether or not there is fraud or overreaching or whether they have done anything untoward, in which event reports will be made and suitable action may be taken." 96 Cong. Rec. 17123 (1951). However, this comment hardly suggests that GAO review was intended to be restricted exclusively to cases of fraud or other improprieties, and amici misconceive what was *part* of Congress' purpose to be its *sole* purpose. See *e.g.*, *United States* v. *Naftalin*, 441 U.S. 768, 774-775 (1979); *United States* v. *Culbert*, 435 U.S. 371, 377 (1978). Furthermore, the terms "overreach," which is defined to include "[t]o get the better of; trick; outwit,"[13] and "untoward," which means "[u]nfavorable; unpropitious,"[14] are fully ap-

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part of the books and records of contractors having negotiated contracts with the Government.

* * * * *

Knowledge that the GAO may later examine these books and records cannot help but make for more careful operations by the Government's contracting officers.

97 Cong. Rec. 13198 (1951). Cf. *Buckley* v. *Valeo*, 424 U.S. 1, 67 (1976).

[13] *The American Heritage Dictionary* 936 (1976).

[14] *Id.* at 1405.

plicable in situations where, as Representative Hardy described them in introducing Sections 2313(b) and 254(c), "[t]he Government representative * * * will * * * be at a tremendous disadvantage" and therefore "the Government will come out on the short end of the deal." 97 Cong. Rec. 13198 (1951).

Likewise, GAO's contemporaneous construction of 10 U.S.C. 2313(b) and 41 U.S.C. 254(c) is not at odds with its present position. Amici rely on the fact that GAO, in letters to Congress on the bill, quoted the preceding statement of Representative Celler on the amendment to the First War Powers Act. See H.R. Rep. No. 791, 82d Cong., 1st Sess. 4-5 (1951); S. Rep. No. 603, 82d Cong., 1st Sess. 4 (1951). As just discussed, however, that statement fully accords with, and surely does not foreclose, GAO's access request to respondent. Moreover, consistent with Congress' consideration of both the War Powers Act amendment and the access statutes, GAO also commented that the access provisions in Sections 2313(b) and 254(c) would be "a deterrent to those persons who might otherwise abuse the authority to negotiate certain contracts without advertising. * * * [A]ny abuses discovered by the General Accounting Office in exercising the authority contained [in the bill] promptly will be brought to the attention of the proper officials, and, if warranted, to the attention of the Congress." H.R. Rep. No. 791, *supra*, at 4-5; S. Rep. No. 603, *supra*, at 4.[15]

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[15] The contemporaneous commentators cited by amici (Am. Br. 15 n.18) in fact support our construction of the access provisions. As GAO Assistant General Counsel Welch stated:

> Another important function of G.A.O. [in addition to settlement of claims] stems from the statutory obligation of certain contracting agencies to include in their negotiated contracts a clause to the effect that the Comptroller General or his authorized representatives shall have

Amici also attribute (Am. Br. 16, 19) great significance to the fact that the Hardy bill containing Sections 2313(b) and 254(c) was amended on the floor of the House to provide a three-year limitations period within which the Comptroller General is entitled to request access to a contractor's records. Representative Burton, the sponsor of the amendment, explained that it was

> not intended to restrict the act but simply to clarify and to write into the bill the well established principle of a time limitation. By writing this into the bill there can be no misunderstanding as to the intent of Congress and this will eliminate the uncertainty of how long records must be kept. It will also tend to serve as notice on contractors that they are expected to preserve their records for this period of time.

97 Cong. Rec. 13375 (1951). Representative Hardy stated that he did "not think that [the proposal was] necessary" but that he did "not have any strong feeling about it" (*id.* at 13199) and that he was "willing to accept the amendment" (*id.* at 13376). Thereafter, the amendment was adopted by a voice vote (*ibid.*). In light of its purpose merely to estab-

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access to and the right to examine any pertinent records of the contractor or any of his subcontractors engaged in performance of the work. * * * The authority derived by G.A.O. from these mandatory contract clauses gives the Office valuable assistance in making an effective and complete audit of contract payments.

G.A.O. does not have the authority to disallow wasteful and extravagant expenditures as such for the simple reason that the procurements involved may be legally valid. However, the Comptroller General may report such procurements to the agency head, to appropriate Congressional Committees, or even to the Congress itself when the circumstances warrant.

Welch, *The General Accounting Office in Government Procurement*, 14 Fed. B.J. 321, 326 (1954) (emphasis added).

lish a limitations period, this amendment does not in any way illuminate the substance of the Hardy bill, and the fact that a limit of three years was selected to coincide with the period of GAO review and settlement of the accounts of accountable officers in the government (*id.* at 13197-13198, 13199) is of little import.

Amici also argue (Am. Br. 21-22) that GAO has previously acknowledged its lack of authority to request records relating to a contractor's commercial business rather than to its contracts with the government. Read in context, however, all of these statements simply reflect the unquestioned proposition that GAO has no independent authority directly to seek access to the records of the contractor's commercial business. Nothing in these documents and testimony suggests that GAO is not entitled to such records where, as here, they are necessary in order to determine the reasonableness of the price set in a government contract containing an access-to-records clause.[16]

Similarly, the "should cost" studies cited by amici (Am. Br. 22-23) have no relevance to GAO's right of access in this case. Such studies entail "comprehensive reviews of contractors' operations" (Am. Br. App. 12a) in order "to evaluate the efficiency and economy of the contractors' operations" (*id.* at 13a) and to determine how much the contractors' products "should cost" the government (*ibid.*). Thus, the focus is on the efficiency of the contractors' business, not on the reasonableness of the relationship between the contractor's costs and the contract price. Because of

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[16] Moreover, the examples noted by amici principally involved "[c]ommercial sales records" (Am. Br. App. 9a) and commercial "production scheduling and shipments" records that "only incidentally, if at all, * * * [pertained to] cost and pricing data for the negotiated contracts * * *" (*id.* at 10a).

the required effort and expense by GAO, these studies are generally undertaken only in connection with a major procurement such as tanks or airplanes. "Should cost" studies, unlike the access provisions, are not confined to negotiated contracts, are "not * * * limited to documents and records pertinent to particular contracts" (*id.* at 13a), and are not restricted to cost and pricing records but extend "broadly * * * to all documents, records, personnel, and other data" (*ibid.*) and "all aspects of operations and management, including but not limited to * * * production systems and controls[,] * * * plant design[,] * * * labor standards[,] * * * quality control systems[,] * * * equipment utilization[,] * * * [and] purchasing and subcontracting procedures * * *" (*id.* at 12a-13a). GAO's recognition that its authority under the access-to-records provisions was insufficient to conduct "should cost" studies in no way undermines its request in this case for access to respondent's cost records necessary to assess the reasonableness of the price charged the government under specific contracts.

For much the same reasons, the statute and bills involving studies of the profits of government contractors, upon which amici rely (Am. Br. 23-24), are inapposite here. The authority at issue there extended well beyond that contained in the access provisions. Among other things, those measures related to the overall profitability of contractors rather than to the protection afforded the government's interest in particular negotiated contracts; directly involved both commercial contracts and government contracts; included advertised as well as negotiated procurements; required the contractor to prepare and submit to GAO such information as GAO concluded was relevant to the profit study; authorized the Comptroller General to obtain subpoenas to enforce his rights pursuant to the study; and empowered the Comptroller General to take sworn statements from the contractor. See Pub.

L. No. 91-121, Section 408, 83 Stat. 208; 115 Cong. Rec. 25793-25801 (1969); S. 2268, 94th Cong., 1st Sess. (1975); S. 3014, 93d Cong., 2d Sess. (1974); S. 2049, 93d Cong., 1st Sess. (1973). Thus, these studies far exceeded the scope of the access-to-records provisions, and the need for additional authority to engage in this type of study does not detract from the Comptroller General's right of access in this case.[17]

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[17] Amici suggest (Am. Br. 8 n.10, 14 n.14, 17 n.20) that the Comptroller General's request for access in this case is invalid because the contracts in question are not subject to the Truth-in-Negotiations Act, 10 U.S.C. 2306(f), or the Renegotiation Act, 50 U.S.C. App. 1211 *et seq.* (which expired effective September 30, 1976; see 50 U.S.C. App. 1212(c)(1)). By their terms, however, the access provisions are applicable to "each contract" (10 U.S.C. 2313(b)) and "[a]ll contracts" (41 U.S.C. 254(c)) negotiated under specified authority, and nothing on the face of the statutes indicates an exemption for contracts that are outside the Truth-in-Negotiations Act or the Renegotiation Act. Moreover, the Truth-in-Negotiations Act, which requires the contractor to submit cost or pricing data in the negotiations process and to certify that these data are accurate, complete, and current, and the Renegotiation Act, which dealt with recovery by the government of excess profits, are directed to specific procurement objectives that are distinct from the purpose of the access provisions—to determine whether the government's interest in reasonable prices has been adequately protected and whether future procurements should be made in the same manner. This distinction between the Acts and the access provisions is reinforced by the legislative histories of the access statutes and the 1951 amendment to the First War Powers Act, which distinguished the responsibility of GAO to review the reasonableness of prices in negotiated contracts from that of the Renegotiation Board to recover excessive profits. See 97 Cong. Rec. 13197 (1951) (remarks of Rep. Hardy); 96 Cong. Rec. 17045 (1951) (remarks of Rep. Case of South Dakota). Finally, amici's argument was not relied on by the courts below and was expressly rejected by the court of appeals in *Eli Lilly & Co.* v. *Staats, supra,* 574 F.2d at 916. See also *Hewlett-Packard Co.* v. *United States, supra,* 385 F.2d at 1014.

Finally, amici assert (Am. Br. 3) that there are no generally accepted accounting principles that would enable GAO to make use of the requested records in order to determine the reasonableness of the contract price. As discussed in our opening brief (Pet. Br. 35-36), the issue of allocating indirect costs, while not amenable to scientific precision, is a familiar accounting question. See also, *e.g.*, W. Behrenfeld, *Accounting Desk Book* 90-92, 118-125 (6th ed. 1980); W. Paton & R. Dixon, *Essentials of Accounting* 496, 510-516 (1958); H. Wright & J. Bedingfield, *Government Contract Accounting* 106, 107-114, 218-230 (1st ed. 1979). There is no insuperable difficulty in developing and employing a method of allocation adequate to assess the reasonableness of the price charged the government.[18] Moreover, in accordance with its standard practice, GAO would discuss the proposed allocation system with the contractor and would furnish a copy of its evaluation and conclusions to the contractor for review and comment prior to public release. Through this process, a fair and reliable methodology can be devised.

CONCLUSION

For the foregoing reasons and the reasons stated in our opening brief, the judgment of the court of appeals should be reversed.

Respectfully submitted.

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Solicitor General

MARCH 1981

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[18] Indeed, an analogous issue of allocation frequently arises in connection with cost-based contracts where the contractor seeks reimbursement for its indirect costs.

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No. 80-264

IN THE

Supreme Court of the United States

October Term, 1980

ELMER B. STAATS, COMPTROLLER GENERAL OF THE UNITED STATES,

AND

UNITED STATES OF AMERICA,
Petitioners,

v.

BRISTOL LABORATORIES DIVISION OF BRISTOL-MYERS COMPANY,
Respondent.

ON WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE SECOND CIRCUIT

BRIEF OF MERCK & CO., INC. AND SMITHKLINE CORPORATION, *AMICI CURIAE*

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BRIEF OF MERCK & CO., INC. AND SMITHKLINE CORPORATION, *AMICI CURIAE*

Merck & Co., Inc. ("Merck") and SmithKline Corporation ("SmithKline") submit this brief as *amici curiae* in support of the judgment of the Second Circuit.

INTEREST OF AMICI CURIAE

1. The *Amici* and Respondent are Similarly Situated.

The *amici curiae* SmithKline and Merck, like respondent Bristol Laboratories Division of Bristol-Myers Company ("Bristol"), are leading pharmaceutical manufacturers. In August

1974, Bristol, Merck, SmithKline and three other pharmaceutical companies were served by the Comptroller General with identical demand letters seeking access to their records relating to a handful of government procurement contracts.[1] In each instance, the Comptroller General's demand was premised on identical standard form access-to-records provisions inserted in their contracts pursuant to 10 U.S.C. § 2313(b) and 41 U.S.C. § 254(c).

Although those statutes and the relevant contractual provisions restrict the Comptroller General to records that are "directly pertinent to" and involve "transactions relating to" the specific procurement contract, the letters served on the *amici* and Bristol made sweeping demands for access to virtually all the records of these companies.[2] The broad scope of the access demands is evident from the government's acknowledgement that GAO is seeking to inspect records of "all costs met in whole or in part from revenues earned on the federal contracts" listed in the demand letters. Pet. Br. 7, *quoting* Pet. App. 9a. As the District Court found in this case:

> "The Government's theory has far reaching implications. The only items excludable from the Comptroller General's reach would be those, if any, which related to costs recovered exclusively from non-government contracts. *** It is undisputed, however, that Bristol does not separately compute the cost of government and non-government contracts or pay for them out of separate funds. Accordingly, *there are no excludable records under*

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[1] *See* Joint Appendix ("J.A.") 20-21; Joint Appendix filed in the court of appeals in *Merck & Co. Inc.* v. *Staats*, D.C. Cir. Nos. 79-1435 & 74-1438 (argued Feb. 11, 1980)("Merck C.A. App.") 49-51; Joint Appendix filed in the court of appeals in *SmithKline Corporation* v. *Staats*, 3d Cir. No. 1464 (filed March 19, 1980)("SmithKline C.A. App.") 60-63. Copies of the joint appendices in the *Merck* and *SmithKline* cases have been lodged with the clerk of this Court.

[2] The Comptroller General's letters demanded access to records "which include but are not limited to (1) records of experienced costs including costs of direct materials, direct labor, overhead, and other pertinent corporate cost, (2) support for prices charged to the Government, and (3) such other information as may be necessary for use to review the reasonableness of the contract prices and the adequacy of the protection afforded the Government interests." J.A. 21; Merck C.A. App. 50; SmithKline C.A. App. 61.

the Government's theory." 428 F. Supp. 1388, 1390 (Pet. App. 9a)(emphasis added).

Like Bristol, both Merck and SmithKline divide their costs into a category of direct manufacturing costs assignable to particular products and another category of unassigned costs, including all research and development, marketing, distribution, advertising and general administrative costs. This common practice reflects the fact that there are no generally accepted accounting principles which permit the accurate and meaningful allocation of the latter category of costs to particular products.[3] Since Merck and SmithKline do not assign costs to particular contracts and do not segregate revenues generated by particular contracts, the interpretation of the access-to-records statute asserted here by the government would encompass *all* of the *amici's* cost records. Indeed, the drastic reach of the identical access demands served on Bristol and the *amici* is illustrated by GAO's expressed inability to define any category of records that would fall outside its demands.[4]

Faced with these sweeping demands, Merck and SmithKline, like Bristol, declined to produce records sought by the Comptroller General and initiated actions seeking declaratory and injunctive relief.[5] The cases initiated by Merck and

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[3] *See* Merck C.A. App. 97; SmithKline C.A. App. 377-92. Petitioner Staats has acknowledged that it would be impossible to ascertain what these pharmaceutical companies' costs are with respect to individual drug items. *See* pp. 25-26 *infra*.

[4] *See* Merck C.A. App. 156, 346-47. Not only has the government failed to identify categories of records that would fall outside its access demand, but GAO has indicated in response to discovery taken in the *Merck* case that it may demand access to records dating back *20 years* or more prior to the date on which the contracts were awarded. *Id.* This testimony is reprinted in Appendix B, *infra*, pp. 5a-6a.

[5] Merck filed suit in the United States District Court for the District of Columbia, *Merck & Co.* v. *Staats*, Civ. Action No. 74-1447 (D.D.C. 1977), *cross-appeals pending*, D.C. Cir. Nos. 79-1435, 79-1438 (argued Feb. 11, 1980), *conditional petition for certiorari before judgment denied*, No. 80-416 (Dec. 8, 1980). SmithKline brought its action in the United States District Court for the Eastern District of Pennsylvania, *SmithKline Corporation* v.

(footnote continues)

SmithKline are presently pending in the District of Columbia Circuit and the Third Circuit, respectively. Given the common origin of the cases brought by these three companies and the important common question of statutory construction they raise, SmithKline and Merck clearly have a direct and substantial interest in this Court's resolution of the issue presented here — the scope of the Comptroller General's access-to-records authority.

2. *Amici* Contend that No Cost Records are Directly Pertinent to the Types of Contracts Involved in these Related Cases.

The position advanced by respondent Bristol in this case, however, is narrower than that presented by Merck and SmithKline in their parallel challenges to the Comptroller General's access demands. Bristol agreed to make available the records of production costs allocated to the specific products purchased under the particular contracts listed in the demand letter. In contrast, Merck and SmithKline have declined to make any cost records available to the Comptroller General. The *amici* believe that, under the access statutes, neither internally allocated costs nor unallocated costs are "directly pertinent" to "the contract" whenever — as in these cases — the contract price was not negotiated on the basis of the contractor's costs and the contractor made no representations about the nature or extent of its costs. This brief places before the Court what *amici* consider to be the proper interpretation of the scope of the access-to-records statutes.

3. The Pending Cases Involving *Amici* Present an Additional Issue Regarding the Lawfulness of the Purpose for Which Access was Demanded.

Unlike Bristol, which focused solely on the excessive scope of the access demands, the *amici* have also contended that the

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(footnote continued)

Staats, 483 F. Supp. 712 (E.D. Pa. 1980), *appeal pending*, 3d Cir. No. 80-1464 (filed Mar. 19, 1980), *conditional petition for certiorari before judgment denied*, No. 80-434 (Dec. 8, 1980).

A fourth company also brought suit challenging an identical access-to-records demand, *Eli Lilly & Co.* v. *Staats*, 574 F.2d 904 (7th Cir.), *cert. denied*, 439 U.S. 959 (1978); and the Government brought suit against a fifth, *United States* v. *Abbott Laboratories*, 597 F.2d 672 (7th Cir. 1979).

Comptroller General exceeded his statutory authority by making these demands for an improper purpose. Rather than using the access authority to audit individual government contracts as Congress intended, the Comptroller General served the demands on Bristol and the *amici* to secure cost data on individual pharmaceutical products sought by two Senators and their staffs and to gather data for an economic study by GAO of the pharmaceutical industry. *See* pp.25-26, *infra*.[6] This issue of GAO's improper purpose, which is not presented by this case, should be reserved by this Court for determination by the two Circuits before which the issue is now pending.[7]

SUMMARY OF THE ARGUMENT

The issue raised by this case is the scope of the Comptroller General's right of access under 10 U.S.C. § 2313(b) and 41 U.S.C. § 254(c) to the records of the thousands of corporations that contract with agencies of the federal government for the supply of an infinite variety of goods and services.

1. The statutory language contains express words of limitation restricting the scope of the Comptroller General's access authority to records that "directly pertain to" and "involve transactions relating to" specific contracts. The contracts on which the GAO premised its access demands to Bristol

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[6] Several commentators have concluded that the access demands served on Bristol, the *amici*, and three other pharmaceutical companies should be unenforceable because they were made for the unauthorized purpose just described. *See* Note, *Eli Lilly & Co. v. Staats: An Undue Expansion of the GAO's Investigatory Power Under the Access-to-Records Statutes*, 74 Nw. L. Rev. 122, 127-30 (1979); Comment, *The Comptroller General's Authority to Examine the Private Business Records of Government Contractors: Eli Lilly & Co. v. Staats*, 92 Harv. L. Rev. 1148, 1152, 1156 (1979).

[7] Merck and SmithKline filed conditional petitions for certiorari before judgment in their respective cases in order to afford this Court the opportunity to address all issues raised by these related cases at one time. In opposing these petitions, the government argued that the improper purpose question presents a distinct issue that should be considered first by the courts of appeals so that "this Court would have the benefit of full explication" of their views before determining whether to examine this question. *See* Brief for Respondents in Opposition in *SmithKline Corporation* v. *Staats*, No. 80-434 at 18.

and the *amici* were fixed-price contracts whose prices were not negotiated on the basis of costs but instead were based exclusively on the contractor's established catalog prices or other evidence of adequate price competition. Application of the statutory words of limitation to this category of contracts demonstrates that no cost records come within the scope of the access-to-records provision. The sweeping interpretation of the statutes proffered by the government, which would require that contractors open virtually all of their business records to government inspection, must be rejected as incompatible with the critical limiting language of the statutes.

2. The limited scope of the authority granted to the Comptroller General by Congress is underscored by the legislative history of the access-to-records statutes. Those statutes had their origin in emergency legislation adopted during the Korean War and were adopted solely to deter "fraud," or "overreaching" or "improprieties" in the negotiation of government contracts. The access authority was intended to accomplish this purpose by "enabl[ing] the Comptroller General to make effective audits" of individual contracts through examination of both the government records and the contractors' books. When, as in the present case, no cost data are submitted during the negotiation process and when the payments to the contractor do not depend on its cost of performance, the contractor's cost records are not "directly pertinent to" the limited audit contemplated by Congress.

3. The restricted scope of GAO's access authority evident from the statutory language employed by Congress and from the legislative history forecloses reliance on any contrary administrative interpretation of the statutes. Even if consideration of GAO interpretations were appropriate, however, this inquiry would not assist the government. GAO's current interpretation of the access-to-records statutes conflicts with GAO's contemporaneous construction of the proposed statute presented to Congress during its consideration of the bill. The new, expansive gloss asserted here also conflicts with GAO's repeated acknowledgements of the limits of its access authority.

4. Contrary to the government's assertion, rejection of its sweeping interpretation of the access statutes would neither

"render meaningless the Comptroller General's right of access" nor "totally defeat his statutory responsibility." Pet. Br. 15. In the past the Comptroller General has used his access authority exclusively to audit cost-based contracts in order to determine the accuracy of cost and pricing data supplied to government procurement officers during the negotation of the contracts. Neither the position advanced by Bristol on the scope of the Comptroller General's access authority nor that asserted by the *amici* presents the slightest threat to GAO's continued performance of its contract audit responsibilities. *Amici* submit only that a manufacturer's cost records are not "directly pertinent" to competitively priced contracts that were not negotiated on the basis of costs.

ARGUMENT

I. UNDER THE PLAIN MEANING OF THE ACCESS-TO-RECORDS STATUTES, NO COST INFORMATION IS "DIRECTLY PERTINENT" TO FIXED-PRICE CONTRACTS THAT WERE NOT NEGOTIATED ON THE BASIS OF COSTS.

As this Court has counseled, "'[t]he starting point in every case involving construction of a statute is the language itself.'" *Southeastern Community College* v. *Davis*, 442 U.S. 397, 405 (1979), *quoting Blue Chip Stamps* v. *Manor Drug Stores*, 421 U.S. 723, 756 (1975)(Powell, J., concurring). Here, the statutes on which the access-to-records demands are based — 10 U.S.C. § 2313(b) and 41 U.S.C. § 254(c) — grant the Comptroller General access only to books and records of the contractor that "directly pertain to," and "involve transactions relating to," the specific "contract."[8] As the District Court found, and the Second Circuit confirmed, these critical phrases are words of limitation that restrict the scope of the access authority granted by Congress. Pet. App. 3a, 10a.

Application of these words of limitation to the specific types of contracts involved in this case and in the related cases involving the *amici* demonstrates that no cost records of these

[8] The statutes are reprinted in Appendix A, *infra*, pp. 2a-3a.

contractors come within the scope of the access provision. As the government has acknowledged, all of the contracts involved in these cases are fixed-price rather than cost-based contracts. *See* Pet. Br. 3. In each instance, there was no actual negotiation of prices; no cost or pricing data were requested by the government purchasing agency in connection with the award of the contract; and the contractor made no representations about its costs in quoting its price for each product.[9] Instead, unlike many "negotiated" government contracts, the contract prices here were established on the basis of the contractors' published catalog prices at which these standard commercial items were sold to the public, or on the basis of other evidence of adequate price competition in the public marketplace. Under the federal procurement statutes, it was unnecessary to submit cost or pricing information in connection with the award of these contracts since competitive market forces established the reasonableness of the contract prices.[10] In these circumstances, the contractors' cost records do not "directly pertain to" or "involve transactions relating to" these contracts.

The Ninth Circuit's decision in *Hewlett-Packard Co.* v. *United States,* 385 F.2d 1013, 1016 (9th Cir. 1967), *cert. denied,* 390 U.S. 988 (1968), recognized that if "costs were not taken into consideration in arriving at the terms and conditions of the contracts in question," and if the proper focus is the specific terms and conditions of the contract that gives rise to the access demand, then records relating to costs "could not be said to directly pertain to, and involve transactions relating to, the contract, as so defined." This is the position that *amici* advance here.

The Ninth Circuit went astray, however, by adopting a strained and unnatural definition of the term "contract." *See*

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[9] Merck C.A. App. 140-45; SmithKline C.A. App. 75-76, 342.

[10] Under the Truth-in-Negotiations Act, 10 U.S.C. § 2306(f), contractors are normally required to submit cost and pricing data to the government as part of the negotiation process. Congress, however, expressly exempted from this requirement the types of contracts involved in these cases — contracts "where the price negotiated is based on adequate price competition" or on "established catalog or market prices of commercial items sold in substantial quantities to the general public."

385 F.2d at 1016. The court inexplicably interpreted "contract" as "embracing not only the specific terms and conditions of the agreement, but also the general subject matter" — "the procurement of described property by the goverment." *Id.* This error expanded the category of information the court considered "directly pertinent to" the "contract."[11]

A fundamental canon of statutory construction is that, "unless otherwise defined, words will be interpreted as taking their ordinary, contemporary, common meaning." *Perrin* v. *United States,* 444 U.S. 37, 42 (1979); *Burns* v. *Alcala,* 420 U.S. 575, 580-81 (1975). The term "contract" has traditionally and commonly been understood to refer to a specific agreement between two parties. *See, e.g., Fletcher* v. *Peck,* 10 U.S. (6 Cranch) 87, 136 (1810); *Larson Construction Co.* v. *Oregon Auto Ins. Co.,* 450 F.2d 1193, 1195 (9th Cir. 1971). Significantly, this same, commonplace definition of contract was contained in federal procurement regulations in force at the time Congress enacted the access-to-records statute in 1951, 32 C.F.R. § 400.201(6) (1951), and it continues to be used in the regulations in force today, 41 C.F.R. § 1-1.208 (1979).[12]

This "ordinary meaning" of "contract" is reinforced here by the manner in which the term "contract" is used elsewhere in the same section of the statute. The mechanism employed by Congress in creating the access-to-records authority was to require the inclusion of an access clause in all "*contracts* negotiated without advertising." Act of October 31, 1951, Pub. L. No. 82-245, 65 Stat. 700 (emphasis added). There can be no doubt that the word "contract" was employed in that phrase to mean a specific, formal agreement between two parties, since

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[11] Nothing in the access provisions themselves or their legislative history justifies this novel interpretation, which has been sharply criticized *See, e.g., Eli Lilly & Co.* v. *Staats, supra,* 574 F.2d at 918-19 (Pell J., dissenting); Note, *Eli Lilly & Co. v. Staats: An Undue Expansion of the GAO's Investigatory Power Under the Access-to-Records Statutes,* 74 Nw. L. Rev. 122, 130-31 (1979); *cf. United States* v. *Abbott Laboratories, supra,* 597 F.2d at 674-75.

[12] 32 C.F.R. § 400.201(6) (1951) provided:

"The term 'contracts' means all types of agreements and orders for the procurement of supplies or services."

only such agreements contain "clauses" and are subject to negotiation. Since it "is hardly credible that Congress used the term [contract] in different senses in the same sentence," *United States* v. *Cooper Corp.*, 312 U.S. 600, 606 (1941), it is clear that "contract" as used in the access-to-records statute refers to the specific agreement between two parties.[13]

Given this "ordinary meaning" of the term "contract," it is easy to apply the statutory restriction that only those records that "directly pertain" to the specific contract may be examined. When the contractor has made no representations to the government purchasing agency about its costs but instead has offered the product at a fixed price equal to or below the price established in the competitive commercial market, the Comptroller General's limited access right does not extend to records reflecting the manufacturer's costs or its pricing methodology.

The government's sweeping interpretation of GAO's access-to-records authority completely ignores the express limiting language of the statute. According to the government, "all costs met in whole or in part from revenues earned" on a particular government contract are within the scope of the access-to-records provision. Pet. Br. 7, *quoting* Pet. App. 9a. The overreaching inherent in this claim is magnified when all revenues are commingled in a general corporate account and are used as required to meet all of a company's ongoing expenses. This is the accounting practice followed by Bristol and the *amici*, and almost certainly by most other government contractors. In this situation, the government's theory encompasses records of all costs "defrayed by the contractor from commingled general revenues that include the government's payments under the contracts." Pet. Br. I.

This interpretation produces absurd results, since the matching of revenues from a particular contract with a manu-

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[13] The legislative history of the access-to-records statute lends further support to this analysis of the meaning of "contract." For example, the sponsor of the access-to-records provision emphasized that the "right [of access] is given [the Comptroller General] in the contract. The right is not given him in the bill." 97 Cong. Rec. 13376 (1951) (remarks of Rep. Hardy); *see id.* at 13198 (remarks of Rep. Hardy).

facturer's range of costs may well be completely arbitrary. For example, a payment received as a result of a given government contract may be used to purchase raw materials for use in manufacturing an entirely different product than that purchased under the contract. The revenue from a sale to the government may become part of an investment in the stock of another corporation, or it may go to pay the salaries of scientists performing research on potential products that may not be marketed for ten years—if ever.

In virtually all cases, the revenues earned on a particular contract will be received after performance. Therefore, they will not relate to the period in which the costs of performing that contract were incurred. This is particularly true for research and development costs in the pharmaceutical industry which of necessity are incurred *many years* before the product is first sold to anyone.[14] The government's construction of the statute thus would permit examination of cost records that not only are unrelated to the contract on which the access demand is premised but also have nothing at all to do even with the product that was procured through the contract.

The District Court found, against this backdrop, that the government's theory is virtually limitless in its sweep, potentially reaching all of the contractor's records relating to all costs of all products. Pet. App. 9a. Since the revenues generated by even the smallest government contract would, as part of the contractor's commingled general revenues, theoretically contribute "in part" to the recovery of all costs, a *single* negotiated government procurement contract would permit the Comptroller General to demand access to all of the contractor's business records.[15] The courts below, therefore, properly rejected the government's interpretation of the access-to-records statutes.

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[14] It now takes, on average, 7 to 10 years to complete the elaborate testing process required by the FDA before a new drug can be marketed. 127 Cong. Rec. S674 (daily ed., Jan. 27, 1981)(remarks of Sen. Mathias).

[15] A senior GAO official acknowledged this consequence of the government's interpretation of the access-to-records provision during a deposition taken in the *Merck* case. *See* Merck C.A. App. 338 (Deposition of Gregory J. Ahart, Director, Human Resources Division, General Accounting Office) (reprinted in Appendix B, *infra*, pp. 5a-6a).

The government's position is in square conflict with Congress' decision to limit the Comptroller General's access only to "directly pertinent" records. *See* Pet. App. 10a. No cost records fall within this limited compass where contract prices are neither cost-based nor negotiated on the basis of costs.

II. THE LEGISLATIVE HISTORY OF THE ACCESS-TO-RECORDS STATUTES UNDERSCORES THE LIMITED AUTHORITY GRANTED THE COMPTROLLER GENERAL.

The legislative history makes clear that the access-to-records provision was enacted for the limited purpose of deterring or detecting abuses in the negotiation process by facilitating GAO audits of individual procurement contracts. In performing the contract audits contemplated by Congress, GAO has no need for access to cost records of government contractors — such as those of the *amici* here — that were not put forward as support for the price and were not used as a basis for computing the payment made by the government. Since these records are not relevant to the detection of misrepresentations in the negotiation of the contract price or of overcharges in the request for payment, they are not "directly pertinent" to the "transactions involving" the contract.

A. The Limited Purpose Of The Access-To-Records Statutes Is Evident From Their Origin In Emergency Legislation.

The access-to-records clauses involved in this case were required by an October 1951 statute. Pub. L. 82-245, 65 Stat. 700.[16] That statute was modeled on, and as originally proposed was identical to, an amendment to the First War Powers Act that had been adopted by Congress in January 1951. Act of January 12, 1951, 64 Stat. 1257. The legislative history of that predecessor statute is critical to a proper understanding of the

[16] The October 1951 statute amended both section 4 of the Armed Services Procurement Act of 1947, 10 U.S.C. § 2313(b), and section 304 of the Federal Property and Administrative Services Act of 1949, 41 U.S.C. § 254 (c), to require the inclusion of access-to-records clauses in virtually all negotiated government procurement contracts. The October 1951 statute is reprinted in Appendix A, *infra*, p. 2a.

Comptroller General's access-to-records authority. *See, e.g., Oscar Mayer & Co.* v. *Evans,* 441 U.S. 750, 755-56, 758 (1979); *Cannon* v. *University of Chicago,* 441 U.S. 677, 694-98 (1979).

The January 1951 amendment to the First War Powers Act was adopted in response to crisis conditions created by the Korean War. Rampant inflation and skyrocketing costs fueled by the war made it difficult for many defense contractors operating under fixed-price contracts to keep their commitments to supply the government with vital munitions. *See* H.R. Rep. No. 3227, 81st Cong., 2d Sess. 3-4 (1950); S. Rep. No. 2686, 81st Cong., 2d Sess. 2 (1950). In response, Congress reinstated the emergency authority created during World War II to negotiate increases in contract prices, but only for an 18-month period. *See* S. Rep. No. 2686, *supra,* at 3; Act of January 12, 1951, § 2, 64 Stat. 1258.

To allay concern about possible abuse of the authority to increase contract prices, *e.g.,* 96 Cong. Rec. 17045 (1951) (remarks of Rep. Marcantonio), Representative Hardy offered an amendment to the bill to provide the Comptroller General with authority to examine "pertinent" records relating to any contracts renegotiated under the statute. *Id.* (Remarks of Rep. Hardy). The bill's floor manager explained that the access-to-records amendment was proposed for the limited purpose of deterring and detecting abuse of the emergency negotiating authority:

> "The amendment will give power to the General Accounting Office to go into the books and delve into the records of these contractors who have been relieved *to determine whether or not there is fraud or overreaching or whether they have done anything untoward,* in which event reports will be made and suitable action may be taken. The power of investigation and inquiry of the General Accounting Office should be an excellent deterrent. These reports also would

be of great help subsequently on the question of renegotiation." *Id.* at 17123 (remarks of Rep. Celler)(emphasis added).[17]

B. The Permanent Access-To-Records Statutes Were Enacted For the Same Limited Purpose.

Shortly after the adoption of the First War Powers Act amendments, Representative Hardy learned that government procurement officers were also negotiating wartime contracts under two permanent procurement statutes — the Armed Services Procurement Act of 1947 and the Federal Property and Administrative Services Act of 1949. *See* 97 Cong. Rec. 13198 (1951). Those statutes lacked any access-to-records provisions. *Id.* "In order to plug this loophole," Representative Hardy introduced a bill to require the inclusion of access-to-records clauses in contracts negotiated under these statutes. *Id.* Both the House and Senate reports echo his explanation that the bill was intended "merely" to "carr[y] into our general procurement statutes the same principle" embodied in the First War Powers Act amendments. *Id.* (remarks of Rep. Hardy); *see id.* at 13199, 13200; H.R. Rep. No. 791, 82d Cong., 1st Sess. 2 (1951); S. Rep. No. 603, 82d Cong., 1st Sess. 2 (1951).

Representative Hardy explained that his "main purpose in offering this bill was to place on the statute books a law which will act as a deterrent to improprieties in the negotiation of Government contracts." 97 Cong. Rec. 13198 (1951). The access-to-records provision was intended to provide such a deterrent by "enabl[ing] the Comptroller General to make effective audits" of the accounts of government contracting officers. *Id.* at 12611 (1951). As he explained:

"[T]he audit which GAO performs is directed primarily to the accounts of the accountable officers of the Government

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[17] This power to detect overcharges reinforced the government's right under the Renegotiation Act of 1951 to recoup payments made for unwarranted costs billed to the government. The government has acknowledged, however, that the Renegotiation Act did not apply to the contracts of Bristol and the *amici* because Congress has exempted contracts for standard commercial items whose prices are set in the competitive market place. 50 U.S.C. App. §§ 1216(e)(1)(A) & (4)(B). *See* Merck C.A. App. 143.

and not to the contractors themselves. The GAO is required by law to take exceptions against accountable officers for erroneous or illegal payments." *Id.* at 13197.[18]

The access-to-records authority was to assist in deterring and detecting erroneous or illegal payments to contractors by enabling the Comptroller General "to check the transaction, both from the Government records and the contractors' books." *Id.* at 13198 (remarks of Rep. Hardy). The access authority thus would serve to safeguard against neglect of responsibilities by government personnel and against such contractor abuses as the inflating of overhead rates quoted to procurement officers during contract negotiations and the improper shifting of costs from fixed-price contracts to cost-plus contracts. *Id.* [19] Where,

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[18] The access authority was intended to focus on auditing the contracting officer's handling of individual contracts. At the time the statute was adopted, GAO's primary function was the settlement of the accounts of government disbursing officers:

> "The central and best known of the GAO's responsibilities was the *audit of expenditure vouchers* (mostly after they had been paid) and the *settlement of accounts* — primarily those of the various disbursing officers scattered around the government — which were required to be submitted periodically along with all their supporting documents. The GAO's checking of individual vouchers was intended to assure that the money was authorized and available, the payment was lawful in every respect, the proper procedures had been followed, *and no fraud or other irregularity was involved.* If any objections were raised, notices of exception were issued to the responsible officers, and unless satisfactory explanation could be made the payments were disallowed." F. Mosher, *The GAO: The Quest for Accountability in American Government* 72-73 (1979) (footnote omitted; first emphasis in the original; second emphasis added).

Commentators writing in the early 1950's, shortly after the access-to-records statute was adopted, noted that the access authority was designed to enable GAO to discharge these audit and settlement responsibilities. *See, e.g.*, Cable, *The General Accounting Office and Finality of Decisions of Government Contracting Officers*, 27 N.Y.U.L. Rev. 780, 782 (1952); Welch, *The General Accounting Office in Government Procurement*, 14 Fed. B. J. 321, 326 (1954).

[19] The examples set forth in the legislative history deal with situations in which inaccurate cost information is supplied by the contractor to the procurement officer in order to obtain a higher negotiated price or an inflated

(footnote continues)

as in the present case, the contractor's cost records did not enter into the negotiation of the contract and were never considered by the government procurement officer in awarding the contract or authorizing payments to the contractor, there is no reason to examine those records in auditing the transaction.

The statements focusing on the statute's limited audit purpose are reinforced by the explanations for two important amendments adopted on the House floor circumscribing the access-to-records authority. Even as originally introduced, the bill was to limit the Comptroller General to "pertinent" records of the contractor "involving transactions related to" the specific procurement contract. During the House debates this language was tightened further to restrict the Comptroller General to records that are "directly" pertinent to the contract. Representative Hoffman, who sponsored the amendment, stated that it was intended "to limit the 'snooping' that may be carried on under the bill." 97 Cong. Rec. 13377 (1951).

The other amendment limited to three years from the date of final payment under the contract the time period during which the Comptroller General may demand access to a contractor's records. In adopting this limitation, Congress demonstrated that it viewed the access-to-records authority as a limited adjunct to GAO's power to audit the accounts of government disbursement officers and disallow erroneous payments, a power also restricted to a three-year period. *Id.* at 13199 (remarks of Rep. Hardy).

These amendments confirm the limited purpose of the access rights to audit the conduct of contract negotiation and the documentation for payment. When cost and pricing records are submitted as part of the negotiation process or in connection with a claim for payment under a cost-reimbursement type of contract, those records are "directly pertinent" to the contract. Through examination of such records, GAO can detect fraud or

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(footnote continued)

payment on cost-based contracts. *See* 97 Cong. Rec. 13198 (1951). One example refers to the setting of the "overhead rate," a cost item, in construction contracts. The government in its brief distorts the legislative history by repeatedly substituting the word "price" where the word "rate" appears in the debates. *See* Pet. Br. at 9, 16, 17.

overreaching by contractors who inflate their cost estimates or who seek payment for costs acutally incurred in connection with other contracts or for which reimbursement has already been obtained. This examination enables GAO to discover illegal or erroneous payments by government contracting officers. By contrast, when no cost data are submitted during the negotiating process, and when contract payments do not depend on the contractor's costs of performance, the contractor's cost and pricing records are irrelevant to the type of GAO audit contemplated by Congress. There can be no fraud or overreaching in the negotiation process where, as here, the contract is awarded on the basis of the contractor's established commercial catalog price for the item. The only records that are pertinent to an audit of fixed-price contracts where costs have never been a subject of the negotiation process are those required to show that the contractor actually had an established catalog price for the item procured and to verify that the sum received in payment from the government was the amount due under the contract.[20]

C. The Government's Interpretation Of The Statutes Conflicts With Their Legislative History.

The government argues that this Court should ignore the express limiting language of the statutes because the legislative history allegedly "makes clear that Congress intended the Comptroller General to have a broad right of access" to evaluate the reasonableness of contract prices and to study the adequacy of government negotiating techniques. *See* Pet. Br. 15, 34. As one commentator has noted, however, and as even the government's brief reveals, there is nothing in the legislative history indicating that the access-to-records authority was designed to enable GAO to evaluate the abstract "reasonableness" of a price and, through that device, to assess the adequacy of government procurement procedures. *See* Note,

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[20] Merck has offered to make such records available so that GAO can confirm that their contracts were properly negotiated on the basis of the catalog price exemption to the Truth-in-Negotiations Act, 10 U.S.C. § 2306(f), and can verify that there were no overpayments by contracting officers. Merck C.A. App. 100-01. SmithKline would be willing to make the same showing.

Government Contracts: Contractor's Obligation to Allow Examination of Records Under 10 U.S.C. 2313(b), 72 Dick. L. Rev. 687, 691 (1968). The absence of any reference to such an "assessment function" strongly suggests that Congress' "purpose was solely to provide a method to discover fraudulent activities and not a means by which government agencies can improve their procurement techniques for use in future contracts." *Id.*

The only "support" offered by the government for the purpose it ascribes to the statute consists of a few carefully edited phrases taken from the House debates and several statements of concern from opponents of the statute. *See* Pet. Br. 15-18. For example, in a misleading effort to create the impression that evaluation of the abstract fairness of contract prices was a concern of Congress, the government on four occasions simply inserts the word "price" into quotations from the legistative history. *See* Pet. Br. 9, 16, 17. As they appear in the Congressional Record, however, the passages excerpted and altered by the government deal only with misrepresentations of *costs* during negotiations. *See* n. 19, *supra.*

Similarly, the government repeatedly refers to the Comptroller General's broad statutory powers to investigate and make reports concerning the expenditures of the executive branch, implying that Congress intended the grant of access authority to be used as an open-ended research "tool" by the Comptroller General. *See* Pet. Br. 8-9, 13, 16-17. Read in context, however, the passage quoted by the government (Pet. Br. 9) refers only to giving GAO the "proper tools" to audit accounts of government contracting officers. No member of Congress ever suggested that the limited access right could be used in connection with the Comptroller General's other, unrelated functions, as now suggested by the government's cropped quotation. In fact, none of the other statutes relied on in the government's brief, 31 U.S.C. §§ 53(a), 60 and 65(a), was even mentioned in the legislative history.[21]

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[21] Those provisions do no more than establish GAO's authority to evaluate the activities of governmental agencies through "management"

(footnote continues)

The statements from opponents of the bill quoted by the government provide no support for its interpretation of the statute. *See* Pet. Br. 17-18. As this Court has repeatedly counseled, statements by opponents "have scant probative value" because, in "their zeal to defeat a bill, they understandably tend to overstate its reach." *National Woodwork Manufacturers Ass'n* v. NLRB, 386 U.S. 612, 639-40 (1967), *quoting, NLRB* v. *Fruit & Vegetable Packers,* 377 U.S. 58, 66 (1964); *accord, Schwegmann Brothers* v. *Calvert Distillers Corp.,* 341 U.S. 384, 395 (1951) ("The fears and doubts of the opposition are no authoritative guide to the construction of legislation."). Moreover, Congress responded to the objections of overbreadth by deliberately confining the access right only to "directly" pertinent records.[22]

The government's interpretation of the access-to-records statute is simply incompatible with (i) its origin in temporary emergency legislation that created a risk of fraud and overreaching, (ii) the deliberate addition of language that narrowed the scope of access, and (iii) the limitation of the access right to the period during which GAO may audit government accounts. These legislative choices would make no sense if Congress had intended to authorize GAO to use the access right to assess and refine negotiating techniques for future government procurement efforts.

III. GAO'S CURRENT INTERPRETATION OF THE ACCESS-TO-RECORDS STATUTES IS NOT ENTITLED TO JUDICIAL DEFERENCE.

The government also argues that the Second Circuit erred in failing to accord substantial deference to what it asserts is

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(footnote continued)

reviews and oversights. They contain no authorization of any kind for the examination of otherwise private records of government contractors. *See* Cibinic and Laskin, *The Comptroller General and Government Contracts,* 38 Geo. Wash. L. Rev. 349, 387-88 (1970).

[22] It was after those expressions of concern that Representative Hoffman (one of the opponents) offered his amendment to restrict the Comptroller General to *directly* pertinent records in order to prevent "snooping" by GAO. *See* p. 16, *supra.*

GAO's "consistent and longstanding construction" of the access-to-records statute. Pet. Br. 22-30. Even if the sweeping position asserted in this dispute were part of a consistent and longstanding interpretation of the statute, it should not prevail, since it conflicts with "the clear meaning of a statute, as revealed by its language, purpose and history." *Southeastern Community College* v. *Davis,* 442 U.S. 397, 411 (1979), *quoting Teamsters* v. *Daniel,* 439 U.S. 551, 566 n.20 (1979). Here, the Court has a "clear duty . . . to reject the administrative interpretation of the statute." *SEC* v. *Sloan,* 436 U.S. 103, 119 (1978).

Moreover, the Court should "accord no special weight" to GAO's current interpretation, because it is actually at odds with the Agency's contemporaneous construction of the statute and with GAO's repeated acknowledgements of the limits of its access authority. *United Housing Foundation, Inc.* v. *Forman,* 421 U.S. 837, 858-59 n.25 (1975). Far from acquiescing in GAO's current view of its access authority, as the government asserts, Congress has acted to guard against the kind of sweeping access demands made by the Comptroller General in this case.

A. GAO's Contemporaneous Construction Of The Statutes Conflicts With Its Position Here.

As this Court has explained, an administrative construction of a statute " 'carries most weight' " when adopted in connection with Congress' consideration of the legislation and when " 'directly made known . . . to Congress in committee hearings.' " *SEC* v. *Sloan, supra,* 436 U.S. at 120, *quoting Zuber* v. *Allen,* 396 U.S. 168, 192 (1969).

Here GAO's contemporaneous interpretation emphasizing the limited purpose and scope of the access-to-records statute was presented to Congress by the Acting Comptroller General during Congress' consideration of the bill. *See* H.R. Rep. No. 791, *supra,* at 4-5; S. Rep. No. 603, *supra,* at 3-4. The GAO's official explanations of the proposal clearly express the agency's

understanding that the access-to-records provision was intended *solely* as a deterrent to improprieties in contact negotiations.[23] The government, inexcusably, fails to mention GAO's contemporaneous construction of the access-to-records provision, which flatly contradicts its current interpretation.

B. GAO Has Repeatedly Acknowledged The Limited Scope Of Its Access-To-Records Authority.

Not only does GAO's contemporaneous construction of the access-to-records statute conflict with its position here, but other intervening GAO statements also are inconsistent with the sweeping access demands made to Bristol and the *amici.*

For example, although GAO now claims that it may examine records relating to the commercial business of Bristol and the *amici* in order to assess the adequacy of government negotiating techniques and the fairness of prices charged the government, GAO has repeatedly stated that it has no authority to demand access to such records. In the 1965 hearings cited by the government (Pet. Br. 26-27), GAO's general counsel testified that GAO had no right to examine records pertaining

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[23] In similar letters to the House and Senate committee chairmen, GAO stated that the "purpose and intended effect of such legislation is clearly explained" in a passage quoted from the House floor debates on the First War Powers Act amendments:

> "Mr. Celler. As I understand the Hardy amendment, the powers given are like a Damoclean sword that will hang over the heads of the contractors whose contracts are changed. The amendment will give power to the General Accounting Office to go into the books and delve into the records of these contractors who have been relieved *to determine whether or not there is fraud or overreaching or whether they have done anything untoward,* in which event reports will be made and suitable action may be taken. The power of investigation and inquiry of the General Accounting Office should be an excellent deterrent." H.R. Rep. No. 791, *supra,* at 4 (emphasis added).

The letters concluded:

> "It is apparent that the proposed legislation herein considered likewise *is intended as a deterrent to those persons who otherwise might abuse the authority* to negotiate certain contracts without advertising." *Id.* (emphasis added).

to "any commercial business" of the contractor.[24] In 1967, the Acting Comptroller General emphasized this important limitation in ruling that GAO personnel could not insist upon examining records relating to a contractor's commercial business, even where review of such records would be necessary to determine whether a catalog-priced item was actually sold in substantial quantities to the general public, as the contractor had represented. GAO Opinion B-162009-O.M. (August 31, 1967) (reprinted in Appendix C. *infra,* pp. 8a-9a). This limitation on records related to a contractor's commercial business has been repeated in other opinions and in testimony to Congress by Comptroller General Staats. *See, e.g.,* GAO Opinion B-141683-O.M. (June 5, 1968) (App. C, *infra,* pp.10a-11a); *Hearings on the Military Budget and National Economic Priorities Before the Subcomm. on Economy in Government of the Joint Economic Comm.,* 91st Cong., 1st Sess. 714 (1969).

GAO also emphasized the limited scope of its access-to-records authority in the late 1960s and early 1970s when it sought expanded authority from Congress in order to perform "should cost" reviews of government contractors. Internal GAO memoranda, which were obtained through discovery in the companion cases in which the *amici* are parties, and which are part of the records in those cases, reveal that in 1970 GAO believed it needed additional authorization from Congress in order to examine a variety of records, including those involving a contractor's "indirect costs" — the very type of records at issue in this case. *See* GAO Memorandum B-159896(.07) (October 22, 1970)(App. C, *infra,* pp.12a-13a). In connection with its request for legislation expanding its access authority, GAO provided Congress with a memorandum emphasizing the limited nature of its access-to-records authority. *See* 115 Cong. Rec. 25800-01 (1969). This memorandum noted that GAO does not have authority to examine a contractor's capital investment data or to attempt to allocate the contractor's capital investment between its defense and non-defense work. 115

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[24] *Hearings on Comptroller General Reports to Congress on Audits of Defense Contracts Before a Subcommittee of the House Committee on Government Operations,* 89th Cong., 1st Sess. 165 (1965) (testimony of Robert Keller).

Cong. Rec. 25800 (1969); *see Hearings on the Military Budget and National Economic Priorities, supra,* 714 (testimony of Comptroller General Staats).

In sum, this litigation is the first occasion on which GAO has asserted the kind of unlimited access authority that it now seeks to uphold.

C. Subsequent Congressional Actions Reveal A Continuing Intention To Circumscribe GAO's Access Authority.

The government asserts that Congress has approved GAO's interpretation of the access-to-records statute by its silence. Pet. Br. 29-30. As this Court has repeatedly counseled, however, "legislative silence is a poor beacon to follow in discerning the proper statutory route." *Zuber* v. *Allen,* 396 U.S. 168, 185 (1969); *see, e.g., Girouard* v. *United States,* 328 U.S. 61, 69 (1946). Here, as shown above, the prerequisite to such an acquiescence argument — a consistent, long-standing administrative construction that has been repeatedly presented to Congress and carefully considered by it — is plainly absent. *Compare SEC* v. *Sloan, supra,* 436 U.S. at 121 ("We are extremely hesitant to presume general congressional awareness of the Commission's construction based only upon a few isolated statements in the thousands of pages of legislative documents") *with* Pet. Br. 24-28.[25]

Actions taken by Congress since the passage of the access-to-records statute in 1951 belie GAO's claim that Congress has acquiesced in an assertion of sweeping authority. On only one

[25] An exchange in the 1965 hearings cited by the government reveals that there was not even passive acceptance of the isolated GAO statements relied upon by the government. *See Hearings on Comptroller General Reports to Congress on Audits of Defense Contracts, supra,* at 649-53. During these hearings, the committee counsel pressed Comptroller General Weitzel to reconcile his view of GAO's access authority with the legislative history of the statute, which demonstrates that the access right, like that granted by the January 1951 amendment to the First War Powers Act, was merely designed to deter "fraud and overreaching." *Id.* at 649-53. The Comptroller General's contention that the October 1951 statute had a "broadened" purpose, *id.* at 652, was disputed by the skeptical committee counsel, *id.* at 653.

occasion has Congress deliberately granted GAO the broad-ranging authority that it has attempted to assert here. As part of the Military Appropriations Act of 1970, Congress authorized GAO to engage in a study of defense industry profits. *See* Pub. L. No. 91-121, § 408, 83 Stat. 208. Significantly, this authority was conferred only for one year, and it was limited to "only a single study." 115 Cong. Rec. 25793 (1969) (remarks of Senator Proxmire); *id.* at 25795 (remarks of Senator Ribicoff). In 1973, and again in 1975, Congress turned a deaf ear to several GAO-drafted proposals that would have authorized GAO to demand broad-based access to contractors' records in order to conduct profit studies of companies having government contracts aggregating more than $1,000,000 during the most recent fiscal year.[26] Since Congress withheld this power when GAO expressly sought it with respect to such large contractors, it is absurd to argue that even broader power regarding all contractors has already been implicitly inserted in the 1951 legislation through Congressional silence.

IV. REJECTION OF GAO'S SWEEPING INTERPRETATION OF THE ACCESS-TO-RECORDS STATUTES WILL NOT IMPEDE ITS ABILITY TO DISCHARGE ITS RESPONSIBILITIES.

The government's *in terrorem* assertion that "the decision below would render meaningless the Comptroller General's right of access and would totally defeat his statutory responsibility" (Pet. Br. 15) is belied by the record in this case and in the companion cases in which the *amici* are parties.

In order to demonstrate the importance of the access-to-records statute, the government submitted an affidavit by GAO's general counsel explaining that in fiscal years 1974 and 1975 GAO's Procurement and Systems Acquisition Division used the access authority to examine contracts and subcontracts totaling $814,900,000, and recovered more than $5,000,000 as a result of overpricing uncovered through its audits. *See* Merck C.A. App. 99-100 (¶ 4). The GAO's answers to interrogatories

[26] *See* S. 2049 and S. 3014, introduced during the 93d Congress, and S. 2268, introduced in the 94th Congress.

in the *Merck* case, however, admitted that *in every one* of those instances GAO was conducting individual audits of *cost-based* contracts in order to determine the accuracy of cost and pricing data supplied to government procurement officers during the negotiation of the contracts. Merck C.A. App. 147. Neither the Second Circuit's decision nor the contentions of Bristol and the *amici* present the slightest challenge to GAO's continued performance of contract audits or to its review of cost information pertinent to cost-based contracts.

Here, however, GAO does not even purport to be using its access authority to audit these particular *non*-cost-based contracts. Merck C.A. App. 146 (No. 8); Brief for the Respondents in Oppositon in *SmithKline Corp.* v. *Staats*, No. 80-434, at 7-8 n.6. Rather, the government has acknowledged that the access demands served on Bristol and the *amici* were issued to obtain data from pharmaceutical companies for use in a study of economic and operational aspects of the drug industry. J.A. 95 (¶ 6). The discovery taken in the *Merck* case revealed that GAO has *never before* attempted to use its access authority to gather data from contractors for such an industry study. Merck C.A. App. 246-81. This case, therefore, hardly presents a challenge to the ability of the GAO to conduct any well-established functions central to its duties.

The government's assertion that the Second Circuit's decision will interfere with GAO's ability to meet its responsibilities is also undermined by the fact that the GAO was pressured into making the access demands served on Bristol and the *amici*. The access demands were made as a result of pressure placed on GAO by two Senators who wanted to obtain raw cost data on individual drug products.[27] Before he acquiesed in persistent prodding to obtain drug company cost records, petitioner Staats had testified that securing such data would not serve any purpose useful to GAO, because "it would be impossible to develop from [the company's] internal accounts what their

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[27] *See SmithKline Corp.* v. *Staats*, *supra*, 483 F. Supp. at 716-17; *Eli Lilly & Co.* v. *Staats*, *supra*, 574 F.2d at 921-22; Note, *Eli Lilly & Co. v. Staats: An Undue Expansion of the GAO's Investigatory Power Under the Access-to-Records Statutes*, *supra*, 74 Nw. L. Rev. at 124.

costs are with respect to an individual drug." *Hearings on Competitive Problems in the Drug Industry Before the Subcomm. on Monopoly of the Senate Small Business Committee,* 92d Cong., 2d Sess. at 8753 (1972).

Petitioner Staats also had advised Congress that no "meaningful conclusions" could be developed on an individual product basis and that use of the access-to-records authority with respect to individual contracts would simply be "a waste of time." *Id.* at 8578. Indeed, rather than claiming a need to use the access-to-records statute "to evaluate the fairness of the contract price" (Pet. Br. 15), petitioner Staats testified that the government's interest in obtaining a fair price is protected by the market when, as here, the government purchases items at or below the catalog price at which the manufacturer sells the product to the public at large. *Id.* at 8580-81. These contemporaneous judgments about his real statutory interests deserve more credence than do the *post hoc* rationalizations of petitioner's lawyers.

CONCLUSION

The judgment of the Second Circuit should be affirmed on the basis of the statutory interpretation advanced above.

Respectfully submitted.

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March 1980

APPENDIX A

Statutory Provisions

1. The October 31, 1951 Access-to-Records statute, 65 Stat. 700, provides:

> Section 304 of the Federal Property and Administrative Services Act of 1949 and section 4 of the Armed Services Procurement Act of 1947 are hereby amended by inserting at the end of the above-named sections the following new subsection:

"(c) All contracts negotiated without advertising pursuant to authority contained in this Act shall include a clause to the effect that the Comptroller General of the United States or any of his duly authorized representatives shall until the expiration of three years after final payment have access to and the right to examine any directly pertinent books, documents, papers, and records of the contractor or any of his subcontractors engaged in the performance of and involving transactions related to such contracts or subcontracts."

2. Section 4(c) of the Armed Services Procurement Act of 1947, 10 U.S.C. § 2313(b), provides:

> Except as provided in subsection (c), each contract negotiated under this chapter shall provide that the Comptroller General and his representatives are entitled, until the expiration of three years after final payment, to examine any books, documents, papers, or records of the contractor, or any of his subcontractors, that directly pertain to, and involve transactions relating to, the contract or subcontract.

3. Section 304(c) of the Federal Property and Administrative Services Act, 41 U.S.C. § 254(c), provides:

> All contracts negotiated without advertising pursuant to authority contained in this chapter, chapter 11C of Title 5, chapter 10 of Title 40, and chapter 11 of Title 44 shall include a clause to the effect that the Comptroller General of the United States or any of his duly authorized representatives shall until the expiration of three years after final payment have access to and the right to examine any

directly pertinent books, documents, papers, and records of the contractor or any of his subcontractors engaged in the performance of and involving transactions related to such contracts or subcontracts.

APPENDIX B

Ahart Deposition Testimony

Excerpts from the Deposition of Gregory J. Ahart, Director, Human Resources Division, General Accounting Office, taken in *Merck & Co., Inc.* v. *Staats,* No. 74-1447 (D.D.C.).

1. *Page 144 (Merck C.A. App. 338)*

Q. Well, we are back to "directly pertinent," again. How direct does "directly pertinent" have to be in order to come within your claim of right? Can you give me some feel for that?

A. Well, in answer to the Interrogatory that we are talking about here, one test is whether or not these affect the prices paid by the Government.

Q. Even though the company may not have taken them into account in establishing a price?

A. Even though the company may not have taken them specifically into account in establishing a price.

Q. The fact that they are there as a general ambient of the company's business is enough to make them directly pertinent to the performance of the contract?

A. In my judgment, that would be.

Q. And this is true even if a company only has one Government contract?

A. Since the access to records clause is brought to bear on an individual contract basis, yes.

2. *Pages 152-53 (Merck C.A. App. 346-47)*

Q. But you are unable, today, to give me any idea what the limitations on the time periods would be, is that correct?

A. Yes, that is correct. The constraints are as I stated but, without more specific knowledge than we possess, we can't be more specific.

Q. So even if costs were not considered in pricing a particular product, conceivably you would insist on the right to

records that might be 20 years old or might relate to costs incurred 20 years ago?

A. If they were determined to be directly pertinent to the contract.

Q. But we have no way of deciding how they might be directly pertinent. There is no way you can define how you would make that test.

A. If they affect the prices, if they are given consideration during the pricing of the—

Q. No, they are not given consideration by the company in making its pricing decision.

A. If they are not given specific consideration, we would have to make a judgment as to whether or not, irrespective of specific consideration, they affect the prices.

Q. In the sense that you described before, that they relate to the company's overall costs and, sooner or later, the company wants to make a profit on a company-wide or division-wide basis?

A. Yes.

APPENDIX C

GAO Opinions and Memoranda

B-162009-O.M. August 31, 1967

Director, Civil Division

Returned. The July 10, 1967, memorandum from Gregory J. Ahart, Deputy Director, Civil Division, requests advice regarding the right of General Accounting Office representatives to audit a Government contractor's sales records to ascertain if in fact the contractor sold substantial quantities of particular catalog items to the general public, thereby qualifying for a permissive exemption from the mandatory cost and pricing data submission and certification requirements imposed on negotiated procurements by 10 U.S.C. 2306(f), Public Law 87-653, the "Truth in Negotiation Act of 1962." In particular, you are interested in examining the manufacturer's sales records which pertain to the catalog sales exemption granted Electronic Associates, Inc. (EAI) of West Long Branch, New Jersey, by the cognizant contracting personnel at Marshall Space Flight Center, National Aeronautics and Space Administration (NASA) incident to the award of contracts number HAS8-15103 of June 30, 1965; HAS8-16789 of November 11, 1965; HAS8-17425 of February 10, 1966; and HAS8-17438 of May 6, 1966, for the purchase of electronic computers and associated equipment.

The letters attached to the July 10, 1967, memorandum show that procurement personnel at Marshall Space Flight Center, before award of the first above mentioned contract, unsuccessfully attempted to obtain detailed sales data for the particular items being procured, in order to independently determine whether the items actually had been sold in large quantities to nongovernment users. In the absence of more comprehensive sales data, the contracting officer was forced to rely upon an overall figure which simply segregated total yearly sales to the Government for all EAI products from total sales to nongovernmental customers and determined on this basis that because EAI had made substantial sales to the public, the contracts could be exempted from the cost certification requirements incident to negotiated procurements.

Under 10 U.S.C. 2313(b) the gist of which was included as paragraph 10(a) of the standard provision of the contracts in question, presumably on Standard Form 32 (Supply Contract), June 1964 edition, representatives of this Office are entitled to:

> "*** examine any books, documents, papers, or records of the contractor, or any of his subcontractors, that directly pertain to, and involve transactions relating to the contract or subcontract."

Commercial sales records do not pertain to or involve transactions relating to government contracts, and we have no right of access thereto under 10 U.S.C. 2313(b).

As to the propriety of the action of NASA contracting personnel in permitting contracts to be negotiated solely on the basis of catalog prices without any showing of substantial sales of the item to the public, it appears that the NASA contracting personnel have violated the criterion established by paragraph 3-807-1(a) of the NASA Procurement Regulation, that catalog price purchases require:

> "* * * positive demonstration by convincing evidence to support the application of this exception. It is not enough that an item be listed in a catalog or price list, or be offered for sale to the general public, or be intended to become a commercial item, but tangible and substantial sales activity must be shown to result from such listing, offering, or intention. * * *"

We interpret this regulation as applying on an item by item basis.

R. F. KELLER

Acting Comptroller General
of the United States

Attachment

B-141683-O. M. June 5, 1968

TO: Mr. Edward Friedman, Procurement, Defense Division

FROM: Mr. Stephen P. Haycock, Assistant General Counsel

Your memorandum of May 9, 1968, raises a question concerning the authority of GAO to review contractors' records with respect to both Government and commercial work under the Defense Production Act, 1950. You state that in connection with a survey Defense Division has accumulated some evidence that contractors are in violation of the priorities system contemplated by the Defense Production Act, 1950, and the Business and Defense Services Administration (EDSA) regulations implementing it. The precise question involved is whether GAO has a right to review contractors' commercial records with respect to production scheduling and shipments of material either under the Examination of Records Clause (Clause 10 of Standard Form 32) or under the authority granted the EDSA under the Defense Production Act, 1950. We understand that Defense Division is interested only incidentally, if at all, in cost and pricing data for the negotiated contracts that may be involved.

In regard to GAO's right of access to records under the Defense Production Act it would appear that no provision of the Act itself grants GAO the right to examine a contractor's commercial records relating to production scheduling, shipments of material or the like. On the contrary, it appears that certain provisions of the Defense Production Act and other legislation militate against any such conclusion. See 50 U.S.C. App. 2155(e) and 2162(c). See also Executive Order 20480, August 14, 1953, set out as a note under 50 U.S.C. App. 2153 and the analysis set forth in a memorandum dated April 21, 1960 (B-141683), by Mr. Masterson to Mr. Ramsey.

With respect to the Examination of Records Clause set forth in Standard Form 32 which apparently is incorporated in the negotiated contracts involved, it would appear that the types of records sought cannot reasonably be considered as

"directly pertinent * * * records of the Contractor involving transactions related to this contract" (Underscoring supplied) [sic]. In B-162009-O.M., August 31, 1967, the Director, Civil Division, was advised that GAO did not have a right of access to a manufacturer's sales records which pertain to the catalog sales exception granted to a contractor pursuant to the "Truth in Negotiation Act of 1962". The present records sought are even more removed from the coverage of Clause 10 of S.F. 32 than were the sales records involved in B-162009-O.M. See, also, B-158349-O.M., April 13, 1966, where it was observed that Fairchild Camera's refusal to provide statistical information relating to the overall financial activities of its Space and Defense Systems Division (which was performing only Federal contracts) was not necessarily contrary to law and that nothing in the law requires a contractor to furnish GAO with listings of its Government contracts or their degree of completion. *A fortiori* it must be concluded that nothing in the law requires a contractor to furnish GAO with records relating to production scheduling and shipments of materials in its commercial business.

B 159896 (.07) October 22, 1970

TO: General Counsel

FROM: Director, DD—C. M. Bailey

SUBJECT: Draft legislation expanding GAO's authority to perform "should cost" type reviews

In your decision, B-159896-O.M., dated September 8, 1970, you advised us that GAO apparently lacks firm statutory authority to perform comprehensive reviews of contractors' operations ("should cost" reviews). In our forthcoming report to the Congress, we intend to point this fact out and to suggest that the Congress may wish to consider expanding our authority in this area.

We believe it would be desirable for us to be prepared when the report is issued to the Congress, about January 31, 1971, with draft legislation that can be considered by appropriate committees. In our opinion, the proposed legislation should provide, as a minimum that:

1. Any contractor holding negotiated contracts valued at $100,000 or more will be subject to review.

2. GAO will have the right to examine into all aspects of operations and management, including but not limited to:

a. production systems and controls

b. plant design

c. labor standards

d. quality control systems

e. equipment utilization

f. indirect costs and controls

g. accounting and cost estimating systems

h. purchasing and subcontracting procedures

i. internal management studies and reviews

3. GAO's rights shall not be limited to documents and records pertinent to particular contracts, but should be broadly interpreted to permit access to all documents, records, personnel, and other data considered necessary to evaluate the efficiency and economy of the contractors' operations.

It would appear to be desirable for these rights to be incorporated into applicable Government contracts and the legislation could, therefore, be drafted so as to amend or replace the current contractual provisions for GAO access to contractors' records.

We would appreciate your drafting legislation to accomplish the objectives described above. Mr. Jerome H. Stolarow, Assistant Director of this Division, is responsible for our "should cost" review efforts and will be available to assist you if further information is needed.